PROBLEMS OF AGRICULTURAL CREDIT IN INDIA

WITH A FOREWORD

BY

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BY

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PREFACE

The problems of agricultural credit and of rural indebtedness are engaging the attention of all who are interested in India's welfare. Real and lasting improvements on the economic condition of the rural population as well as the rehabilitation of Indian agriculture on sound lines depend fundamentally upon an erradication of rural indebtedness coupled with ensuring a proper supply of credit to agriculture at reasonable charges. The inauguration of the Reserve Bank of India has brought about an orientation of the entire problem of agricultural credit. Having personally worked with a bank, I have tried in this volume to offer concrete suggestions as to how the Reserve Bank can help in the solution of this knotty and pressing of all problems by linking itself to the existing rural credit supplying institutions as well as by providing directly for the supply of agricultural credit. I have also embodied in the following pages the substance of the lectures which I delivered before the Bengal Economic Society of the University of Calcutta on the same subject.

In the preparation of this volume my thanks are due to Dr. H. L. De, D.Sc. (London.), Dr. P. Datta, Ph.D. (London.), Mr. S. K. Lahiri and others who have helped me considerably. I am also profoundly grateful to Mr. G. W. Tyson, Editor, "Capital", for kindly writing a foreword to my humble work.

CALCUTTA,
June, 1937

B. B. GHOSH

FOREWORD

Dr. B. B. Ghosh has asked me to write a short foreword to his book on agricultural credit and I have much pleasure in doing so, firstly because of my personal friendship with him and further on account of the painstaking research which I know he has devoted to this subject. The sudden awakening of the public conscience of this country to the problem of rural indebtedness and rehabilitation is one of the most striking manifestations of the outlook of the new India. This new mental attitude is not in any way a monopoly of Congress or the more advanced political parties and it is in my opinion an excellent thing that young Indians, well qualified, are voluntarily devoting much time and thought to a problem which pervades every department of India's economy. The information which is contained in the following pages is of very real value to everyone who approaches the question of agricultural indebtedness and rural uplift. The essentials of what is a highly complicated subject are set forth with an economy of words and a notable clarity of thought. I have great pleasure in commending it to all who have India's welfare in their daily thoughts.

Geoffrey William Tyson
Editor, "*Capital*".

TO

DR. R. C. MAJUMDAR, M.A., PH.D.

VICE-CHANCELLOR, UNIVERSITY OF DACCA.

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INTRODUCTION

Agriculture is the principal economic undertaking in India, and three-fourths of her population depend upon agriculture for their livelihood. In any scheme for the economic uplift of India, agriculture should naturally occupy a very prominent place.

Agriculture in India is confronted with numerous difficulties of which the following deserve special mention. The appalling poverty of the rural population is a striking feature. Though there are no reliable data, giving particulars of the cost of production, the value of produce raised and the income of the agriculturists from subsidiary occupations, it may be roughly estimated that the average income of an agriculturist in British India will be round about Rs. 42 a year. Like in every other country, nature exercises a powerful influence on cultivation in India, and the Indian Agriculturists are in a large measure subjected to the vicissitudes of the seasons. Compared with that of other countries agricultural productivity in India is remarkably low.

Small and uneconomic holdings coupled with fragmentation of the same constitute a powerful bane of Indian agriculture. The cultivators in all parts of India are steeped in indebtedness. The inadequacy of subsidiary occupations to supplement the slender income of the cultivators is a regrettable feature of our rural economy. The economic depression causing a collapse of commodity prices has hit Indian agriculture hard, which proves clearly that the Indian agriculturists is not immune from the influence of markets, both national and international, but, unhappily, he is not equipped with the necessary organisation and credit facilities to help him as in countries like the United States of America, Canada, Denmark, Germany and other European countries. Lack of proper organisation among the cultivators in India for the purpose of acting together in matters of credit and marketing often prevents them from getting a fair price for their produce. Illiteracy is another serious handicap from which the Indian agriculturist suffers, and in the absence of any rapid development of general education of the masses technical education in agriculture is not likely to make much headway. In spite of the lowering of the margin

of profit from cultivation the Indian agricultist continues to incur wasteful expenditure owing to tradition, and social and ceremonial customs. Land as a form of security has lost much of its value in most places owing to the restriction of rights of cultivators in land by various hereditary customs and paternal legislation. All these factors combined have produced cumulative evils, resulting in low credit-worthiness of the Indian agriculturist who is compelled to borrow at high rates of interest. The bulk of his profits goes to constitute the payment of interest, leaving thereby no incentive for improvement. In fact, "agriculture in India is carried on as a mode of living rather than for profit."

Agriculture is an industry and, like other industries, requires both short-term and long-term finance. But there are certain fundamental differences between industrial and agricultural finance. One-man concern is the unit of production in agriculture, and hence the credit available for the concern is limited to the resources of one man or one family. The modern method of raising credit by subscription through the mechanism of joint-stock enterprise is not accessible to agriculture. The industrialist can

capitalise the future, or raise money on estimated earning power, but the cultivator cannot, there being no commercial measure of these expectations in agriculture acceptable to the ordinary investor. Hence, the industrialist can raise his capital by subscription, while the agriculturist can only do so by credit. Agricultural production is characterised by inelasticity of supply and comparative difficulty of adjusting itself to demand. The agriculturist is often isolated and remote from the normal opportunities for obtaining credit. Compared with those of the industrialist, his operations are complex, long in their cycle and subject to exceptional risks from weather and disease beyond the ordinary ups and downs of prices and wages from which he suffers in common with industrialists. His capital is normally sunk in forms of wealth, difficult for any one but an expert to value and not readily chargeable as security for an advance, while his personal training and method of life are not such as to fit him to overcome these natural disadvantages and to establish that position in the credit market to which his financial stability and high standard of honesty generally entitle him. Unlike industrialists, who can control price by withdrawing a part of

their supply from the market owing to their ample resources and credit facilities, the cultivators are not able to hold on to their crops for better prices, owing, mainly, to the lack of credit facilities. In India they must dispose of their produce immediately the harvest is over, being compelled to do so by their poverty, ignorance and debt obligations. The apparatus of commercial banking is not available to agriculture, more so in matters of long-term credit. Land and other forms of real property being the securities, which can be offered for the purpose of long-term credit, commercial banks avoid investing their funds in long-term credit in agriculture, because the above kinds of securities are deemed by them to be so much frozen assets. Commercial banks must preserve the liquidity of their assets. Besides, land as a form of security has been at a discount in India, owing to the various difficulties in connection with titles and restrictions, customary or statutory, on the right of transfer. These important differences between agriculture and other industries give rise to special problems of rural finance requiring special treatment.

Agricultural finance can well be regarded as deserving of special state aid in view of the

vital significance of agriculture in the life of any nation. Agriculture is not merely a business, it is also a public service, performed by the cultivators in the national interest. Agriculture is, therefore, invested with a clear and unquestionable public interest, and its status is a matter of national concern necessitating deliberate and far-sighted national policies, not only to conserve the natural and human resources involved in it, but also to provide for national security, encourage prosperity, and secure social and political stability.

Among others, the credit needs of the agriculturists are fundamental, and may be broadly classified under three main heads, namely, short-term, intermediate and long-term. It should, however, be remembered that the cultivator sometimes requires credit, which may be either short-term or intermediate or long-term, (i) for marketing and movement of produce, and (ii) for small rural and cottage industries. The distinction between short-term and intermediate credits is very thin, and for our purposes the two may be studied together. In India the cultivator requires short-term and intermediate credits to meet current outgoings and facilitate production and marketing, and these credits

partake of a seasonal character. Short-term loans are generally utilised for the purpose of buying cattle, agricultural implements, manures, and seeds ; for financing current expenses of a cultivator's household ; and for payments of *kists* and allied obligations. These short-term loans are usually repaid immediately after the crop is raised, and are only prolonged in case of a partial or a total failure of crops. Intermediate credit, which goes generally towards the purchase of cattle and farming implements, is normally for a longer period, varying from one to three years. In India the cultivator requires long-term credit for obtaining fixed capital, which is used for redemption of debts, reclamation of land ; for the purchase of new lands and more expensive implements ; for consolidation and improvement of holdings and similiar other purposes.

With the steady growth of population causing thereby more pressure upon the soil, the necessity for long-term funds is gradually increasing Because in order to maintain a larger population, more intensive cultivation requiring greater capital is being constantly resorted to. The long-term loans should generally be repayable from the margin of profit of the

borrower's holdings, and the instalment system of repayment is, therefore, spread over a long term of years, varying from 20 to 30 years in India. (This limit is adopted by the majority of land mortgage banks in India). The maximum period allowed for repaying such loans is, 30 years in Finland, 33 years in Chile, 36½ years in New Zealand, 42 years in Australia, 50 years in Italy and Japan, 54½ years in Austria, 57 years in Switzerland, 60 years in Denmark, 63 years in Hungary, 68½ years in Ireland and 75 years in France.

Short-term and long-term credits have their own peculiar and distinctive problems. Longterm funds require a technique of lending, payment and collecting as distinct from those of the short-term, and as such demand a different treatment.

In addition to the above kinds of short-term and long-term loans, which may be called productive rural credits used as they are for productive purposes, Indian agriculturists not infrequently undertake loans for unproductive purposes. For example, Indian agriculturists are proverbial spendthrifts in social and religious ceremonies. In marriages, *sradh* ceremonies and the like they spend a huge amount of money, and the loans obtained for these purposes are

either short-term or long-term, the latter being more common.

The problem of the supply of agricultural credit is one of the most pressing of all problems. The very inherent nature of the agricultural industry has made its credit low, owing to its inability to provide any tangible, liquid and easily marketable security. The position has been rendered still worse after the economic depression, which has brought about a colossal collapse of agricultural prices. In India the credit of the cultivator has been further affected by his inability to pay his old debts, by the series of enactments passed in various provinces to restrict the sale or transfer of rights in land, and by several measures of debt adjustments, voluntary and compulsory. In spite of all these drawbacks and handicaps, Indian agriculture has been supplied with finance through various credit agencies, however crude and oppressive may be the methods employed by a few amongst them.

The sources from which agricultural credit is supplied are :—

(1) Indigenous banks.

(2) Money lenders (including sellers on credit), both professional and non-professional.

(3) Co-operative organisations.

(4) Land mortgage banks.

(5) Government.

(6) Commercial banks (including the Imperial Bank of India), the exchange banks and other joint-stock banks.

(7) Loan offices in Bengal.

(8) Nidhis and Chit Funds in Madras.

The indigenous banking system consisting of money-lenders, shroffs and the like forms an important credit agency in the Indian banking system and constitutes an integral part of India's rural economy by providing the bulk of the credit needs of Indian agriculture. In several parts of India they are even to-day. the only source of credit. The difference between shroffs and money-lenders is that the former use borrowed money either in the form of deposits from the public or by drawing and discounting hundis, while the latter work generally with their own capital. Cases are not rare, where the village mony-lender borrows at times from the urban money-lender or the city shroff. Some of the indigenous shroffs and bankers work

generally on modern lines and transact all kinds of business which the ordinary joint-stock banks perform including the issue of pass books and cheque books. But unlike the joint-stock banks, they do not publish any balance-sheet and their management is entirely controlled by a single proprietor or a firm of proprietors. For the sake of convenience, a distinction will be made in the course of this study between the money-lenders and the indigenous bankers, the former consisting of those whose primary business is not banking but money-lending. The indigenous bankers include all banks other than the Reserve Bank of India, the Imperial Bank of India, the joint-stock banks and the co-operative societies, and they consist of any individual or firm receiving deposits and dealing in hundis or lending money. It should however be mentioned that there are several classes of money-lenders who receive deposits, while there are certain banking communities which have been given the name of bankers and are regarded by the public as such for all purposes though they do not receive any deposits. Money-lenders may be either professional or non-professional, the latter consisting of land-lords, well-to-do agriculturists, pleaders, pensioners, widows, etc., who usually

lend mony to those whom they know fairly well and on good security which consists generally of land or ornaments. The Provincial Banking Enquiry Committees attempted to obtain all available statistics in regard to money-lenders and indigenous bankers, but their reports show that reliable statistics are not available regarding the capital employed by money-lenders and indigenous bankers. But this much can be said that amongst the agencies financing agriculture. the indigenous bankers are the most important.

Co-operative banks are established under the Co-operative Societies Acts, the Co-operative Societies Act, 1912, being the basic Act ruling throughout India except in Bombay and Burma, where local legislation in 1925 and 1927 respectively supplanted the Act of 1912. The co-operative banks consist of the provincial banks at the apex, the central banks which are affiliated to the provincial banks, and the primary societies which are mostly affiliated to the central banks. The co-operative banks and societies are prevented by their governing Acts and Rules from lending to anyone who is not a member of the institution, except with the previous sanction of the Registrar. The primary societies are mostly agricultural, and their main function is to provide the cultivators

with credit, and educate them in the principles and practices of co-operation and thrift. The provincial banks help the central banks by advancing funds for use as part of their working capital, and also by the grant of ordinary and special cash credits. The provinal banks derive their capital mainly from deposits of the public, and the central banks and the primary societies also contribute to the capital of the provincial banks in the form of share capital and deposits of their surplus funds. The provincial banks are also entitled to derive funds from the Imperial Bank of India in the shape of cash credits and overdrafts on the guarantee of their respective Provincial Governments, the amount of such funds being fixed for each province. The central banks provide their affiliated primary societies with the requisite working capital. They obtain their funds partly from the provincial bank, and partly from deposits by the public. The bulk of shares of the central banks are held by the affiliated primary societies. A few successful central banks have also been able to build up substantial reserves. The primary societies maintain a register of assets and liabilities of each individual member, and a copy of this is

deposited with the central bank. The agricultural primary societies are generally of unlimited liability. In this place useful reference may be made to the numerous non-agricultural societies both with limited and unlimited liability. They are rendering useful services to different classes of persons, including officers of Government, employees of industrial companies, small traders, artisans, shop-keepers clerks, petty contractors, wage earners, etc. From the point of view of banking, the co-operative urban banks are very prominent among such urban societies. These co-operative urban banks, which are generally of limited liability, draw their funds largely from deposits, and they generally finance the small trader and the small industrialist. Recently they are encouraging the growth of small industries founded on co-operative basis by providing the latter with finance. Like in some European countries, the co-operative urban banks are transacting regular banking business, e.g., cash credits, cheques, bills, clearing and remitting business. In spite of many set-backs, the co-operatative movement in India has made remarkable progress, which is evidenced from the following figures. But be it remembered here that

notwithstanding this progress of the co-operative movement, it has only touched the fringe of the vast problem of India's rural economy, and more speed should be imparted to the movement for the benefit of our rural population.

Class A. Banks with Capital and Reserve of Rs. 5 lakhs and over.

At the end of the year	No.	Capital & Reserve (in lakhs of Rs.)	Deposits & Loan received (in lakhs of Rs.)
1925-26	10	91	5,38
1926-27.	12	1,12	7,01
1927-28.	16	1,50	8,53
1928-29.	18 (*a*)	1,63	9,01
1929-30.	22 (*a*)	2,05	10,90
1930-31.	26 (*a*)	2,50	12,56
1931-32.	31	2,89	14,81
1932-33	32	3,29	17,55
1933-34	31 (*b*)	3,20	16,55

(*a*) Excludes one bank in Burma, statistics of which are not available.

(*b*) Excludes one bank in Hyderadad amalgamated with another.

Class B. Banks with Capital and Reserves of Rs. 1 lakh and over but less than Rs. 5 lakhs.

At the end of the year	No.	Capital & Reserv (in lakhs of Rs)	eposits & Loan Received (in lakhs of Rs.)
1925-26.	104	2,03	9,30
1926-27.	119	2,25	11,98
1927-28.	126	2,49	13,17
1928-29.	141	2,78	14,99
1929-30.	157	3,08	16,13
1930-31.	169	3,31	17.54
1931 32.	173 (*c*)	3,36	17,01
1932-33.	184	3,72	19,47
1933-34.	192	3,99	14,06

The land mortgage banks which have been recently started under the aegis of the co-operative movement in the Punjab, Madras, Bombay, Bengal, Assam and various other provinces in India are yet few in number. They are very useful institutions for the purposes of long-term credit, the redemption of mortgages of land, the clearance of debt and land improvements. In 1930 there were 68 land mortgage banks in India with a membership of 14,142 thousands and a total working capital of 4,696 thousands of rupees.

(*c*) Excludes one bank in the U. P. and another in the C. P, statistics of which are not available.

The Government grant *takavi* loans to cultivators for agricultural operations, land improvement, and other prescribed objects. The Govenment provide but a very small portion of the finance required by agriculturists in the shape of loans under the Land Improvement Loans Act and the Agriculturists Loans Act, which empower the local Governments to grant loans to the agriculturists from state funds. The delay involved in the disposal of such loan applications and the levy of illegal gratifications coupled with strictness in realisations and other difficulties have rendered these loans very unpopular, and the meagre amount of such loans actually given to the agriculturists may be realised from the following figures, compiled by the Central Banking Enquiry Committee. The Government also finance agriculture to a small extent by purchases of debentures of land-mortgage banks in several provinces, and by giving loans to co-operative societies for specified objects.

(In thousands of rupees.)

Provinces.	Land Improvement Loans Act	Agriculturists Loans Act	Period
Assam	7	1,50	Average of five years.
Bengal	93	14,44	Relating to 1928-29
Bihar and Orissa	70	8,34	Average of five years.
Bombay	13,72 (in 1926)	9,57 (Average of normal years)	Figures for each type of loan not separately available for one year.
Burma	20 (ordinary year)	1,90 (Average of ten years.)	
Central Areas	1.70	1,58	Average of three years.
Madras	12,70	11,54	Relating to 1927-28.
The Punjab	5,00	11,00	Average of five years.

The Governments of almost all progressive countries have recognised their responsibility in the matter of agricultural credit, and it may be interesting to note in this place how agricultural credit has been receiving attention, especially after the "Agricultural Crisis", from the State in several countries. In Great Britain, under the Small Holdings' and Allotments' Act of 1908 the Government of Great Britain were empowered to take all land which any one individual owns in England and Wales in excess of 50 acres, and to lease or sell it to a farmer at a cheaper and convenient price. The Government fulfilled this task through the County Councils. Any

labourer or farmer could purchase a holding from a County Council, by paying in cash a sum not less than one-fifth of the price ; one-fourth could be secured by a perpetual rent charge redeemable in the manner prescribed by English Laws ; the balance could be secured by a mortgage to be paid off half-yearly in instalments of principal and interest or by terminable security. The maximum period allowed for such a credit was 60 years. The Government of Great Britain provided the Scottish Board of Agriculture with a large sum of money to enable the latter to carry on its work of land reform under the Act of 1911, which empowered the Scottish Board of Agriculture not only to adjust rights of tenants on land, but also to enlarge small holdings and to acquire estates for sub-division and allotment to small holders. The inauguration of the Agricultural Mortgage Corporation Ltd. in England under the Agriculturists Credit Act of 1928 is a memorable event in the rural history of England. The Government of the United States of America have adopted extensive measures to help agricultural credit. For example, three distinct banking systems, namely, the Federal Reserve Banking System through rediscount of agricultural paper, the Federal

Intermediate Credit System by grants of loans for periods not less than 6 months and not more than 3 years, and the Federal Farm Loan System through loans ranging up to 40 years have been helping agricultural credits. The Congress has further provided, under the Agricultural Marketing Act of 1921, for the constitution of a revolving fund by a grant of 500 million dollars to be administered by the Federal Farm Board in order to advance loans to co-operative associations engaged in the marketing of agricultural products. Germany legislated in 1932 for the relief of agricultural debt in the encumbered estates, and for the taking over of certain debts and for the management of accounts by the Prussian Co-operative Bank. Under the Decree laws of 1933 and 1934, the National Agricultural Credit Bank of France was entrusted with a considerable fund for financing the wheat harvest through its affiliated regional agricultural credit banks, and advances were also given to wheat marketing societies by the National Agricultural Credit Bank under certain conditions. Legislation was passed in Italy in 1932 reorganising agricultural and mortgage credits, and agricultural banks. The Italian Government introduced non-co-operative credit along with co-operative

credit by capital and interest contributions as well as by long-term and short-term loans. In 1932 the Japanese Government legislated authorising the Central Bank to give credit to the co-operative societies, to make special advances for capitalisation, and provided for indemnification by the State in case of any loss incurred in these operations. Argentina legislated in 1932 for a rural credit section in the Bank of Argentina with the object of improving the organisation and distribution of rural credits, agricultural co-operation and rationalisation of rural industries. Provision has been made in the Australia's Commonwealth Bank (Rural Credits) Act 16 of 1925 to enable the latter to finance agriculture adequately through the Rural Credits Department, attached to the Bank. The Union of South Africa has provided for an extensive system of agricultural and other forms of rural credit through numerous "Agricultural Loan Companies" and "Rural Credit Societies" with the "Land and Agricultural Bank" at their top. The Dominion of New Zealand annexed a "Long Term Mortgage Department" to the New Zealand Bank by a special enactment in 1926 for the provision of long-term agricultural finance. Even China passed a law in 1934,

which constituted the first recognition of co-operation in Chinese national economy.

The commercial banks, including the Imperial Bank of India and the exchange banks, play little part in the direct supply of agricultural credit in India. These banks do not consider agricultural finance as part of their ordinary business. They, however, finance agriculture indirectly by financing traders who give advances to small village dealers; some banks also lend directly on the security of produce, valuables and mortgage. A few banks grant advances to landlords and to the more substantial cultivators on personal security with sureties or on the security of produce or of gold. The Imperial Bank of India was formed in January 1921 by the amalgamation of the three presidency Banks of Bengal, Bombay and Madras, and it was governed by the Imperial Bank of India Act, No. XLVII of 1920 till the first of April, 1935, when the Imperial Bank of India Amendment Act was passed. Hitherto it possessed certain functions as a bankers' bank; e.g., most of the leading banks in India kept their cash balances other than till money with the Imperial Bank of India; it managed the Clearing Houses. They will be henceforth managed by

the Reserve Bank. It also acted as the Government Bank. Owing to its privilege of being a bankers' bank as well as a Government Bank, the Imperial Bank of India was subjected to several restrictions in matters of making loans or advances ; it was generally prohibited from transacting any foreign exchange business, and it could not transact any business not specified in the above Act. In addition, the Government exercised control over the bank in several ways, e g., in matters of appointing four Governors to the Central Board, the two Managing Governors (on the recommendation of the Central Board), and the auditors, etc. The Government also could issue "instructions to the Bank in respect of any matter, which in their opinion vitally affects their financial policy or the safety of Government balances." In order to increase the banking facilities in India and to develop the habit of banking and investment among the Indian population the Imperial Bank of India was bound by a statutory obligation to open not less than 100 new branches within the first five years of its inauguration. This obligation was duly fulfilled. The Imperial Bank of India has undoubtedly made serious efforts to

develop banking in India both in the towns and the rural areas. In addition to several branches, it has also opened many pay offices and out-station offices at small centres of trade. Besides the three local head offices and 161 branches, there are 3 sub-agencies, 26 pay offices and 21 out-station offices of the Bank.

The inauguration of the Indian Reserve Bank has deprived the Imperial Bank of its privilege of being a bankers' bank and a Government bank. The new amendment has converted the Imperial Bank of India into a commercial bank and henceforth it can transact all kinds of banking business which an ordinary joint-stock bank may perform, including the business of foreign exchange, and it has also been made free from many of the restrictions which had been hitherto imposed upon it.

Commercial banking in India is undertaken by the Imperial Bank of India, the foreign exchange banks, the Indian joint-stock banks and many of the indigenous bankers. After a chequered history the Indian joint-stock banks have come to occupy to-day a prominent place in the economic life of the country. By the end of 1933 there were 54 joint-stock banks

in India with a capital and reserve of Rs. 5 lakhs and over. Of these the Central Bank of India, the Allahabad Bank, the Bank of India, the Bank of Baroda, the Punjab National Bank, the Bank of Mysore, the Indian Bank, the Punjab and Sind Bank and the Punjab Co-operative Bank had deposits of Rs. 1 crore and over. The deposits of the first four exceeded Rs. 5 crores in each case. Like in other principal countries of the world, commercial banks render a most valuable economic service to the country. In India the bigger joint-stock banks transact the ordinary banking business and, among other services, receive deposits and make loans and advances, including the discounting of bills. "They also take part in the movement of produce from the village to the exporting port and in the distribution of imports from the ports of entry to the distributing centres." So far as the agriculturists are concerned these banks only deal with the larger landholders, the planting community and others who possess tangible and marketable security. The smaller banks generally advance loans to the professional money-lenders and agricultural classes, and their business is mainly that of a loan office. Tnough one or two Indian joint-

stock banks participate in foreign exchange business, their turnover is very small. They do only participate in the "financing of India's foreign trade from the stage at which exports leave her ports, or to the stage at which imports arrive thereat." The Indian joint-stock banks follow the conservative English principles of banking, and hence give loans usually for short periods and against certain forms of security. They do not, therefore, take any material part in the financing of Indian industries, unlike the German or Continental Banks in Europe.

Capital, Reserves and Deposits of Indian Joint-stock Banks.

Class A. Banks with Capital and Reserves of Rs. 5 lakhs and over.

At the end of the year	No. of Banks	Capital and Reserves Rs. (lakhs)	Deposits Rs. (lakhs)
1925	28	10,60	54,49
1926	28	10,84	59,69
1927	29	11,08	60,84
1928	28	11,10	62,85
1929	33	11,54	62,72
1930	30	11,85	63,21
1931	33	12,03	62,23
1932	34	12,21	72,34
1933	34	12,34	71,67

Class B. Banks with Capital and Reserves of Rs. 1 Lakh and over but less than Rs. 5 lakhs.

At the end of the year	No. of Banks	Capital and Reserves Rs. (lakhs)	Deposits Rs. (lakhs)
1925	46	1,18	3,41
1926	47	1,26	3,47
1927	48	1,22	3,46
1928	46	1,20	3,50
1929	45	1,15	3,58
1930	54	1,37	4,31
1931	51	1,24	3,84
1932	49	1,21	3,82
1933	50	1,21	4,64

The principal business of the exchange banks, which are all non-Indian, is the financing of India's foreign trade. Owing to lack of general banking facilities in India the foreign exchange banks have been gradually undertaking the internal banking business of the country, and to-day they occupy a prominent place in the general banking system of India. They receive deposits both on current and savings bank account, receive fixed deposits, buy bills in foreign currencies, advance money against shipping and other documents and finance the imports of bullion. They also finance the internal trade to a certain extent. In 1870 there were only 3 such banks; in 1880, four, and since 1922

eighteen foreign exchange banks have been working in India. Their head offices are located outside India, and they represent various financial interests, e.g., English, American, German, Japanese, etc. In their earlier years, the sums employed by these exchange banks ,were drawn mostly from abroad, but during recent years they have been attracting an increasing volume of deposits in India, which mounted up to about Rs. 70,78 crores in 1933.

The loan offices were originally started in Bengal on the lines of land mortgage banks. They usually attract funds by deposits. The main function of the loan offices is to lend money not only to landlords, bnt also to actual cultivators against the security of land or any other valuables. Personal security is also very popular with loan offices. Though a few of them finance tea gardens, generally they do not finance trade or industry. Some of them combine money-lending with trading, but this practice is fast dying out. Then Calcutta loan offices advance money against Calcutta house property. Some of them do commercial banking, grant loans against crops in godowns or in transit. In Bengal there were 782 loan offices at work in 1929 ; their paid-up capital is generally small,

and only 13 have a paid-up capital of Rs. 1 lakh or over.

Mention may be made here about the Nidhis and Chit Funds in Madras. Originally started as mutual loan societies the Nidhis have gradually developed into "semi-banking" institutions." They take deposits either in the "form of deposits proper, or of withdrawable share capital paid in monthly instalments, and they make loans for all purposes." Though loans are usually made to members, surplus funds may be available to non-members, too.

The "Chit Fund" is a loose organisation of a small number of people and serves as a very useful mechanism for facililating savings, which are pooled together to be used by the members in various ways. The Chit Funds exist mainly in "the south and south-west of the Madras Presidency, and to a lesser extent in other parts." A large number of Chit Funds is also found in the Travancore State.

The establishment of the Reserve Bank of India constitutes a land-mark in the history of agricultural credit in India, and the role which the Reserve Bank can profitably play in the economic life of Indian agriculturists will occupy our attention in subsequent chapters.

In spite of the numerous credit agencies which supply Indian agriculture with finance, the problem of agricultural credit in India remains acute, and continues to tax the imagination and resources of legislators, economists and reformers for a practical solution. In a critical analysis, the problem resolves itself into various forms. An uneven and unequal distribution of agricultural credit is a striking Phenomenon. Plethora of funds is lying idle in some areas, while others are suffering from paucity of credit provisions. The inelastic character of the supply of agricultural credit is evidenced by its lack of adjustment to the seasonal variations in demand. It is frequently found in several areas that the agriculturist has no access to funds which are plentiful in supply, because he is unable to offer suitable forms of security, personal or otherwise. Lowness of personal credit due to low productivity of Indian agriculture is a serious handicap confronting the agriculturist in obtaining necessary loans. The various credit agencies are loosely organised without any co-operation and co-ordination among them. The consequence is unequal distribution of various credit institutions over different parts, bewildering fluctuations and variations in rates of interest, forms

of security, and methods of payment, collection and realisation. In the following chapters we shall examine how far it is possible to reorganise agricultural credit in India, by modifications and amendments of existing credit institutions, or by inaugurating new and modern credit agencies wherever required so that the Indian agriculturst may be assured of a regular supply of adequate credit at reasonable prices under proper safeguards. Along with this reform of credit agencies, steps should be taken through a constructive agrarian policy to improve standards of agricultural production in India, so that the credit of the agriculturist may be enhanced in the money-market. Agricultural problems must be attacked on all fronts.

CHAPTER I

SHORT TERM CREDIT

In the absence of reliable statistics regarding agricultural production, sale and distribution, it is not possible to frame any accurate estimate of the requirements of the cultivators of credits of various classes. Some of the Provincial Banking Enquiry Committees devoted attention to the calculation of short-term and intermediate credits required by cultivators in India. For example, the Madras, Bombay and Burma Committees gave the following estimates :—

	Estimated amount of short-term loans (Rs. crores)	Estimated total of rural indebtedness (Rs. crores)
Madras	70	150
Bombay	32·5	81
Burma	20	50-60

Though the Central Banking Enquiry Committee did not venture to put forward even a rough estimate of the cultivators' requirements of short-term and intermediate working capital, they infer that a figure of 300 to 400 crores of

rupees may be taken as a lower limit for the whole of British India. The Committee appreciate the difficulty of even making a rough estimate of the long-term credit requirements of the cultivators. On the basis of the calculation of the Provincial Committees regarding the total rural indebtedness in India at a sum of Rs. 900 crores, the Central Banking Enquiry Committee guessed that if Rs. 400 crores out of this total of Rs. 900 crores represent short-term and intermediate credits, at least Rs. 500 crores should represent the requirements for long-term credit which the cultivators should have in order to pay off old debts. But it should be remembered that various items of expenditure, e.g., for improvements of land and cultivation, purchase of building, provision of irrigation works and the like, have been left out of account in the above estimates. The expenses under the latter items would amount to a considerable figure, because the cultivated acreage of land in India is more than 200 millions. It may however be pointed out that the recent report of the Agricultural Credit Department of the Reserve Bank of India goes to maintain that the volume of indebtedness has increased still further since then. Measured in

terms of commodities, it must now be almost twice as much as a result of the fall of prices since 1929.

Short-term credit needs of the agriculturists in India may be classified under two main heads, namely, (i) loans given for seasonal agricultural operations, e.g. purchase of seeds, manures, implements, etc., and (ii) loans for marketing and movement of crops. These loans are usually made for periods not exceeding a year. The agriculturists also require loans for the purpose of cattle and more expensive implements. These are generally for periods not less than one year and more than 3 years, known as intermediate credit.

In the following pages, we shall examine how the existing credit agencies are meeting the short-term and intermediate credit needs of the agriculturists in India, and try to suggest new lines of improvement for the re-organisation of the supply of short-term credit for agriculture. It should be pointed out in this place that the various credit agencies financing the agricultural industry in India usually supply both short-term and long-term credits, except the land mortgage banks and the other forms of co operative

organisations which finance long-term and short-term credits respectively. Though commercial banks do not as a rule invest their moneys in loans of long periods, there are a few doing this business.

The creation of the Reserve Bank of India has brought about a new orientation of the problem of agricultural finance in India, and it will be useful to examine the whole question in the light of this new institution. Under the provisions of the Reserve Bank of India Act the Bank has been authorised to help the supply of agricultural credit, directly and indirectly.

Sec. 17 (2) (b) of the Reserve Bank of India Act provides for "the purchase, sale and rediscount of bills of exchange and promissory notes, drawn and payable in India and bearing two or more good signatures, one of which shall be that of a scheduled bank, or a provincial co-operative bank, and drawn or issued for the purpose of financing seasonal agricultural operations or the marketing of crops, and maturing within nine months from the date of such purchase or rediscount, exclusive of days of grace." Sec. 17 (4) provides for "the making to States in India, local authorities, scheduled banks

and provincial co-operative banks of loans and advances, repayable on demand or on the expiry of fixed periods not exceeding ninety days, against the security of......(c) such bills of exchange and promissory notes as are eligible for purchase or rediscount by the Bank; (d) promissory notes of any scheduled bank or a provincial co-operative bank, supported by documents of title to goods which have been transferred, assigned, or pledged to any such bank as security for a cash credit or overdraft granted for *bona fide* commercial or trade transactions, or for the purpose of financing seasonal agricultural operations or the marketing of crops." The Bank has also been invested with powers of direct discount. Sec. 18 provides that when in the opinion of the Central Board, or where the powers and functions of the Central Board under this section have deen delegated to a committee of the Central Board or to the Governor, in the opinion of such committee or of the Gevernor as the case may be, a special occasion has arisen making it necessary or expedient that action should be taken under this section for the purpose of regulating credit in the interests of Indian trade, commerce, industry and agriculture, the Bank may, notwith-

standing any limitation contained in sub-clauses (a) and (b) of clause (2) or sub-clause (a) or (b) of clause (3) or clause 4 of section 17, purchase, sell or discount any of the bills of exchange or promissory notes specified in sub-clause (a) or (b) of clause (2) or sub-clause (b) of clause (3) of that section though such bill or promissory note does not bear the signature of a scheduled bank or a provincial co-operative bank; or make loans or advances repayable on demand or on the expiry of fixed periods not exceeding ninety days against the various forms of security specified in clause (4) of that section. "Provided that a committee of the Board or the Governor shall not, save in cases of special urgency, authorise action under this section without prior consultation with the Central Board and that in all cases action so authorised shall be reported to the members of the Central Board forthwith."

Thus we find that the Reserve Bank of India has been authorised to finance agricultural operations and marketing through the mechanism of rediscount of bills for a period not exceeding nine months, and this facility can only be obtained from the Reserve Bank through a scheduled bank or a provincial co-operative

bank whose endorsement on such bills is an essential condition for their rediscount by the Reserve Bank. The Reserve Bank is also authorised to give loans or advances to scheduled banks or provincial co-operative banks against the security of promissory notes of such banks provided these promissory notes are supported by documents of titles to goods which have been pledged with those banks as securities for cash credits or overdrafts for genuine commercial and trade transactions, or for the purposes of seasonal agricultural operations, or marketing of crops. Such credits given by the Reserve Bank of India are repayable on demand or on the expiry of ninety days. Any short-term credit in agriculture given for periods not exceeding ninety days cannot help much in matters of actual agricultural operations. The utility of such loans either directly or in forms of bills consists in their ability to finance the marketing of the agricultural products, and the advantage of such accommodation from the Reserve Bank of India will only be available to the agricultural industry in proportion to the improved marketing technique adopted in agriculture. Even in the case of the financing of agricultural paper of

nine months' usance, the advantages, which the Reserve Bank can pass on to the agricultural industry, depend upon two vital factors, namely, the development of a bill habit among those engaged in the agricultural industry, and the easy accessibility and close proximity of the scheduled banks or the provincial co-operative banks to those who are engaged in agriculture either as primary producers, traders, bankers, or middlemen.

It is, therefore, essential that we should make a critical analysis of the various credit supplying agencies in agriculture before we can assess the potential utility, which is likely to accrue to the agriculturists from the Reserve Bank of India in the provision of credit facilities. An examination of the marketing organisation of the agricultural industry is also fundamental.

The Co-operative organisation is the most suitable machinery for providing agriculturists with finance. The financial solvency of the entire co-operative movement depends among other factors upon the soundness of the provincial apex banks, which supply finance to the agriculturists through the central co-operative banks, financing in their turn the primary societies.

The Imperial Bank of India provides the provincial and some of the central co-operative banks with cash credits and overdraft on the security of the promissory notes of the various co-operative societies. During recent years, however, the Imperial Bank of India has been continually reducing this kind of loans to the co-operative banks, and at present it does not want to advance money except on the security of more liquid assets, because promissory notes of co-operative societies, being ultimately backed by land, are not in favour with the commercial banks as good forms of security. Provincial banks are also entitled to cash credits from the Imperial Bank to a specified extent on the guarantee of their respective provincial governments.

Under the Reserve Bank of India Act, 1934, the co-operative organisations can obtain accommodation from the Reserve Bank in two ways. For example, the provincial co-operative bank is entitled to rediscount agricultural bills with the Reserve Bank, maturing within nine months of such rediscount and the provincial bank can then pass on its funds thus obtained from the Reserve Bank to central co-operative banks and other primary

societies. In practice this provision will enable the co-operative banks to derive short-term finance from the Reserve Bank if the Reserve Bank gives adequate facilities to the co-operative banks to supplement their resources by rediscount of agricultural paper on reasonable terms and thus enable them to meet their requirements in the busy season. This provision must not be treated as emergency provision intended to enable the co-operative banks to tide over some unforeseen difficulties. It is normal agricultural credit that co-operative banks expect from the Reserve Bank and not merely emergency credit. But this provision is not likely to be of much practical benefit to the agriculturists for a long time, because the mechanism of bills of exchange through which this credit facility can be secured from the Reserve Bank is as yet undeveloped in India, more so in rural areas.

The other provision of the Reserve Bank of India Act is that which authorises the Reserve Bank to make loans or advances to provincial co-operative banks or scheduled banks on the security of their promissory notes, backed by titles to goods pledged with such banks for loans to be secured. Such credits given by the Reserve Bank of India are repayable on demand or on

the expiry of ninety days, and are therefore useful only for the marketing of agricultural produce. Even such credit facilities can be fully utilised by the agriculturists, provided marketing has been improved through unions of producers, co-operation of traders, development of warehouses, etc., as discussed in the following pages.

In both cases, whether the credit obtained is for nine months or ninety days, the agriculturists can only benefit, provided there is a close and active link between the provincial co-operative banks and other forms of co-operative societies. Generally speaking, the agriculturists deal directly with the primary credit societies, which obtain funds from the central co-operative banks, financed in their turn by the provincial apex banks. If the central banks must obtain facilities through the provincial banks, it may cause unnecessary delay and inconvenience, and it is, therefore, suggested that direct link should be established between the central co-operative banks and the Reserve Bank. It is, of course, true that everything is not well with each and every central bank. Hence it is desirable that the Reserve Bank should prepare a list of those central banks which

will be entitled to accommodation from the Reserve Bank directly in the same way as a provincial co-operative bank. The test of including a central bank in the list should be based upon soundness and a minimum amount of working capital, the details of which should be left to the Reserve Bank to decide. In case of extending such facilities to central co-operative banks, the Reserve Bank ought to possess some control over them through audits and checks as suggested in subsequent pages.

The Reserve Bank of India Act (Sec. 17,4, d) restricts the power of the Reserve Bank to making loans or advances against the security of promissory notes of a scheduled bank of a provincial co-operative bank supported by documents evidencing titles to goods only in cases where such promissory notes are taken for "cash credit" or "overdraft'. It will be useful to include within the scope of this provision promissory notes for loans or advances as well.

Sec. 17, 2a of the Reserve Bank of India Act empowering the Reserve Bank to purchase, sell and rediscount bills and promissory notes arising out of commercial and trade transactions excludes the provincial co-operative banks from

its scope and confines itself only to scheduled banks. It is desirable to include the provincial banks within its scope, and also the list of the central co-operative banks as suggested before. The urban co-operative banks are fast developing, and some of them are doing modern banking business. The urban co-operative credit societies with limited liability are primarily intended to finance small traders, artisans and others who are engaged in small industries. The urban co-operative credit societies are financed by provincial co-operative banks through the central co-operative banks. The consumers' stores, industrial and trading societies like sugar factories and handloom weaving societies, the milk supply unions and the like are beginning to grow in India, and it is highly desirable that they should be duly financed by the urban co-operative institutions. It is therefore desirable to amend the Reserve Bank of India Act in the way suggested above.

Sec. 17 (a), (c) of the Reserve Bank of India Act empowering the Reserve Bank to purchase, sell or rediscount bills of exchange and promissory notes issued for the purpose of holding or trading in securities of the Government also excludes the provincial co-operative banks from

its scopes and confines itself exclusively to scheduled banks. The provincial co-operative banks all over India have large holdings in Government securities, and buy and sell them for their constituent central co-operative banks and their individual members, and hence they should be embraced within the scope of this provision.

The Reserve Bank should not only re-discount agricultural paper bearing the signature of approved co-operative banks, but should also extend to them the same facilities as to scheduled banks regarding remittance of money by mail or telegraphic transfers between the accounts kept by its offices, branches or sub-offices.

The scheduled banks can obtain accommodation from the Reserve Bank of India by rediscounting bills, maturing within ninety days or nine months, and in forms of loans or advances on the security of their promissory notes, backed by titles to goods deposited with them for cash credit or overdrafts for periods not exceeding ninety days. This facility which the commercial banks are able to obtain from the Reserve Bank may come to the use of the agriculturists provided the commercial banks are closely linked to those engaged in the agricultural

industry. In actual practice the commercial banks take little direct part in financing agriculture. Whatever finances they provide for rural areas are mainly directed towards financing agricultural marketing except in Great Britain where penetration into the country-side of the branch banking system has rendered it possible for the commercial banks to provide a large volume of rural credit. The bulk of the commercial banks in several other European countries takes but little direct part in the supply of agricultural credit in spite of a well-developed branch banking system. The uneconomic nature of the majority of the holdings, the slender nature of the security that the agriculturist can offer account partly for the Indian joint-stock banks not having provided any substantial amount of rural credit, while other deterrent factors consist mainly in lack of branch banking in India, and an undeveloped bill market. Before the countryside can be strewn with a net-work of branches of the commercial banks, steps should be taken to utilise the latter in the service of short-term agricultural credit. The scheduled banks should come into close touch with the co-operative organisations. A close link ought to be

established between the scheduled banks on the one hand and the central co-operative banks on the other. The latter should be allowed the privilege of obtaining discount facilities and loans from the scheduled banks on certain specified conditions. Rural credit is now provided by the commercial banks mainly in forms of loans to the various rural credit agencies. The money-lenders and indegenous banks obtain loans from the commercial banks either by cash credits or by discounting hundis, cash credits being more common. The bulk of agricultural credits supplied by commercial banks go towards the financing of the marketing of agriculture. The traders in agricultural produce are generally financed by the commercial banks. In the following pages we shall suggest how the improved methods of marketing and the establishment of licensed warehouses can make it easier for the commercial banks to finance agriculture in India.

It should be remembered here that the co-operative provincial, central and primary credit banks as well as the commercial banks are the most suitable machinery for financing short-term credit needs, because they cannot

afford to lock up their resources in long-term loans consistent with safety. They must preserve the liquidity of their assets. It is therefore suggested that the above mentioned credit institutions should confine their business exclusively to short-term loans. The present practice of some of the central co-operative banks of doing both short-term and long-term credit business is highly unsatisfactory, and should be discouraged. The unification of the two kinds of business in one institution is likely to cause confusion and irregularities, because the short-term and long-term loan transactions require different technique and treatment. The separation of the two functions is fundamental, if the central co-operative banks are going to be linked to the commercial banks and the Reserve Bank of India.

In its recent report, the Agricultural Credit Department of the Reserve Bank of India has made some valuable suggestions for the reorganisation of the co-operative movement in India, and it is worth examining them critically. The co-operative movement must tackle the problem of overdues which are large almost everywhere, and have become for all practical purposes long-term loans. The causes of these overdues

are manifold. In the past the co-operative societies tried to liquidate the long-term indebtedness of their members with their short-term deposits and got their assets frozen into long-term loans, which can only be repaid, if at all, in small instalments spread over a long term of years. Overfinancing, failure to take prompt measures in case of defaults and the fall in commodity prices during the last quinquennium further accentuated the situations. Before the co-operative societies can be made to discharge effectively their proper functioning of advancing short-term credit, their assets, which represent these long-term loans, should be separated and disentangled from their other business. Unless this can be done the Reserve Bank can be of little assistance to the co-operative banks. Long-term finance is not the function of a commercial bank and still less of the Reserve Bank. Agricultural paper representing the renewals of old loans is not suitable for rediscount by the Reserve Bank. Even in view of the existing long-term commitments of the co-operative banks the Reserve Bank may be unwilling to rediscount freely agricultural paper, which represent genuine short-term financing. The suggestion to transfer the long-term loans of the

co-operative banks to the land mortgage banks is strewn with many practical difficulties. So far as they are beyond the capacity of the debtor to repay even in prolonged instalments, they must be clearly written down, and even so reduced the debts may prove too wide-spread and complicated for the land mortgage banks to deal with. Land mortgage banks are only recent growths, and even in Madras where they are most developed they are not nearly co-extensive with central co-operative banks or credit societies. In some areas the debts outstanding against individual members are far in excess of the maximum which land mortgage banks are authorised or which they should be authorised to advance. A serious handicap would be imposed upon these new institutions if they are burdened from the beginning with a clientele which has proved persistent defaulters. The land mortgage banks will, no doubt, finance the members of the co-operative secieties to liquidate their long-term loans where it is safe and possible to do so, but under present state of affairs such relief will only affect an insignificant proportion of the members. The real solution seems to lie in another direction. The central co-opera-tive banks must scale down the debts to a level

where there is a reasonable prospect of repayment out of the profits of agriculture within a reasonable period, say, twenty years. The irrecoverable portion must be written off from their reserve and other funds. The sale of a portion of the member's property may be necessary in certain cases. Advantage should be taken of the present easy conditions of the money market and the low rates of interest in order to put the above measures into immediate effect and prevent the arrears accumulating.

In future care should be taken to avoid overdues. It is not possible to stop the farmer falling into arrears when he is unable to meet his obligations owing to a crop failure, which is of frequent occurrence in several parts of India. The co-operative societies should arm themselves with ample reserve funds by working on a sufficient margin of profit in order to meet the contingency of bad seasons. In the majority of cases the co-operative societies are found to be working with incredibly low margins of profit, and the difference between their borrowing and lending rates is very narrow. They cannot work successfully unless there is a liberal margin of profit in good years and large reserve funds are accumulated for bad years.

The management of the co-operative societies take immediate measures to stop overfinancing, unpunctuality and defaults. Proper principles of co-operation should be propagated, stricter official control, better inspection and control by the central banks ought to be encouraged. It is fundamental to introduce more practical bankers within the movement, managed as it is now mostly by amateurs. A close contract should be established between the co-operative movement and commercial banking. Wherever possible the movement should utilise the services of local business and banking talent. A great check may be imposed upon the societies if more adequate representation of the depositors could be secured on the Boards of the Provincial or the Central Co-operative Banks either by election or nomination. The nature of business which the societies should be allowed to transact may well be restricted, and the Agricultural Credit Department of the Reserve Bank of India even suggests that advances for any purpose whatever, which cannot reasonably be expected to be repaid in one year should be ruled out beyond the sphere of co-operative societies, at least at their present stage of development. This means that loans should be strictly limited to cultivation

finance, which means expenses incurred in connection with ploughing, sowing, weeding, etc., and even the sums ordinarily required for the maintenance of the farmer's family till harvest. Overfinancing may be checked to a large extent if the co-operative department and the central banks obtain an approximate estimate of the crop yield and the normal cost of cultivation with the help of the Settlement Reports and the Agricultural and Revenue Departments. Loans should not be normally given for more than two years, and provision should be made for their repayment in equal instalment. Such loans should be kept separate from the annual loans and should form only a small portion of the total business of any society. Loans should preferably be given by instalments. Strictness ought to be observed regarding repayment and extension for repayment should only be allowed in cases of crop failure certified by the Department and then only if there are reasonable prospects of recovery in the near future.

If the co-operative societies deal only with short-term finance leaving the farmers to resort to the money-lenders for financial accommodation of other kinds the danger may arise that the money-lenders may take away the entire crop

for realising their dues leaving the societies without any means for realising their loans. Hence, some legal provision is necessary to secure them prompt payment out of the gross produce at harvest. The all-India Co-operating Act, of course, confers upon the societies a prior claim over the crop in case of loans for seeds or manure, and in case of loans for the purchase of cattle and implements, over the articles so purchased. It does not, however, create a definite charge over the property, and the Maclagan Committee rightly points out that the provision is largely inoperative "partly owing to the difficulties in proving that a particular crop has been grown by means of a particular loan and partly owing to a ruling of the Calcutta High Court which allows an outside decree-holder to attach a crop in priority to a society unless the society also obtains a decree in its favour". The above Committee recommended that the prior claim should be definitely described as a charge so that it should operate against outside attachment or sale even in the absence of a decree in favour of the society. The Bombay Act makes any debt given by the society a charge on the crop as well as on the stock-in-trade like cattle, implements, etc.,

of the borrower. It, however, protects the *bona fide* purchaser because "a charge entitling a society to follow up produce or its proceeds in the hands of *bona fide* purchasers is likely to result in reluctance on the part of purchasers from dealing with the produce of co-operation except at a discount". This raises the whole legal and practical difficulty of relying on a hypothecation and not a pledge. The Calvert Committee has suggested a way out of the difficulty. The borrower would be allowed to dispose of his produce freely and leave the *bona fide* purchaser unaffected, but it would be deemed an offence for the borrower to utilise the sale proceeds without first paying off the society's debts subject to the prior claims of land revenue and rent. The Agricultural Credit Department of the Reserve Bank of India suggests that the Co-operative Societies Act might be so amended on the lines of the English Agricultural Credits Act of 1928 as to give the societies a fixed charge or agricultural charge upon produce obtained with the aid of loans advanced by them, and to render liable to three months' imprisonment any cultivator-borrower who disposed of his produce without repaying this loan. In order to prevent abuses, it may

be provided that no prosecution under this Act can be started without the previous sanction of the Registrar of Co-operative Societies. The mere existence of such an Act would react most favourably upon the psychology of the farmers and tend to impart a more healthy tone to the co-operative movement.

The agricultural bills which will be re-discounted with the Reserve Bank for accommodation of funds may be merely finance bills not backed by any tangible security except that of the personal goodwill of the endorser. In actual practice the necessity of drawing such finance bills will be very great especially in financing agricultural operations, and this method should be encouraged by the Reserve Bank with due checks and balances.

The direct participation of the Government in providing agricultural credit is insignificant, nor is it very practicable. The real scope for state action lies in helping indirectly the supply of rural credits through the reorganisation of the various credit agencies and the pursuit of a rational agrarian policy, the details of which are suggested in subsequent pages.

In spite of many odds the money-lender still persists as an important feature of Indian rural economy owing to his simple and elastic methods of business, his personal touch with the borrowers, his local knowledge and experience. The gradual decline of the money-lenders may be attributed to the general economic depression, the protection given to the agricultural borrower by laws such as the Land Alienation Acts, the Usurious Loans Act, the Agricultural Debtors' Act, the Civil Procedure Code, etc., the growth of co-operative societies, the delay in the matter of awarding decrees, and the suspicion against the questionable practices of some of them. Notwithstanding their services to agriculture, the continuance of the money-lenders as such is not desirable, owing to their usual high charges of interest, unscrupulous methods of business in the majority of cases, the temptation of easy and facile credit given by them, and the sooner their place is taken by the modern financing agencies the better. In the meantime steps ought to be taken to modernise the practices of the money-lenders and to safeguard the interests of the Indian agriculturists. In this connection we should

suggest compulsory licensing or registration of money-lenders operating under specified conditions, e.g., fixing the maximum rates of interest for each province, standardisation of their methods subject to proper control and audit either by the Government or by the Reserve Bank. The licensed money-lenders should be encouraged to advance loans as far as possible against receipts issued by warehouses and agricultural hundis. It is necessary thus to utilise the money-lenders to create that large amount of self-liquidating agricultural paper which the country needs for the efficient working of its banking and currency systems. They should confine themselves exclusively to money-lending, combination of both money-lending and trading being prohibited. The licensed money-lenders should be entitled to the procedure already in force for the recovery of public demands for the recovery of loans made against agricultural hundis and warehouse receipts. They should be allowed to obtain advances from the commercial banks on the security of their agricultural paper, and should be given the same remittance facilities as are allowed to other banks by the Reserve Bank of India.

The commercial, the central co-operative and the provincial co-operative banks should extend to the licensed money-lenders all facilities for the discount of their agricultural bills. They should be allowed to continue both their existing short-term and long-term loan transactions, but they should be compelled to keep separate books for the two kinds of business. Any private money-lending except under a license should be made punishable by law. By improving their methods of business on modern banking lines, the licensed money-lenders will inspire confidence and will be able to increase their volume of business with the commercial banks. They will thus benefit indirectly from the Reserve Bank of India by rediscounting their bills with the latter through the scheduled banks, which will endorse all their (money-lenders') papers.

It should be pointed out here that during recent years from amongst the agriculturists has grown a new class of agriculturist money-lenders. They are wealthy agriculturists who have adopted extensive business of money-lending. Their methods of business, rates of interest and modes of realising debts are no less unsatisfactory than the professional money-

lenders. Being agriculturists they are exempted from all preventive legislation applying to the professional money-lenders. It is suggested to treat them equally as any other money-lender and the above recommendations should also apply in their case.

In its report the Agricultural Credit department of the Reserve Bank of India further recommends that the Provincial Governments should consider the establishment of village Panchayat Courts for settling minor money suits. This would benefit both the agriculturists and the money-lender by providing an inexpensive and simple machinery for the expeditions adjudication and recovery of debts.

The indigenous bankers constitute the most important element in the rural credit machinery. The bulk of agricultural credit is provided by them. The indigenous banks usually finance the agriculturist indirectly through the village money-lender or the Sahukar. They finance both short-term and long-term loans required for agricultural operations as well as marketing. The merchants and traders derive their funds from the indigenous bankers, who advance credits either in forms of cash or hundis.

The method of doing their business is very simple. Their accounts are kept in a simple and economical manner. They are easily accessible, and they have a personal knowledge and experience of those with whom they deal. We have already observed earlier in our discussion how the practices of the indigenous bankers vary from very primitive ways of transacting loan operations to modern banking like buying and selling remittance, discounting hundis. receiving deposits, advancing loans against stock-in-trade, issuing cheque books, etc. Most of the indigenous bankers also combine trading with their banking business.

In the Reserve Bank of India Act, 1934 no provision has been made to include them within the scope of the Reserve Bank. In view of the fact that the indigenous banks control the bulk of the capital of all credit agencies supplying rural areas, small traders and industrialists with finance, it is imperative that a link should be established between the Reserve Bank of India and the indigenous bankers. Unless the latter can be brought into close touch with the modern money-market through the Reserve Bank of India, the Reserve Bank will never succeed in

exercising a full and effective control over credit, and the organisation of the indigenous banks is an essential priliminary for the development of a full fledged bill market in India. In order to make facilities of modern banking available to rural areas, attention must be concentrated upon the indigenous banks. It is much easier task to provide the rural areas with a net-work of indigenous bankers already possessing a local knowledge and experience through their re-organisation than to attempt opening numerous branches of commercial and co-operative banks in order to cater for the credit needs of the agriculturists.

There exists now a very thin link between the indegenous banks and the modern joint-stock banks, the latter being reluctant to do extensive business with the former, because the methods of business employed by indegenous banks are not easily intelligible to the commercial banks. Besides, the indigenous banks tend to cloak accounts and financial position under a veil of secrecy. The indegenous banks at present meet all the credit demands made upon them from their own capital, and in periods of extreme stress and strain they go to the commercial

banks for accommodation. The commercial banks usually keep with them a list of approved shroffs, who may obtain accommodation under specified conditions, either in forms of cash credits or hundis. During very busy seasons, some approved shroffs are also entitled to credit facilities from the Imperial Bank of India through rediscounting hundis. Under existing conditions the Reserve Bank can only come to the help of indigenous banks indirectly through the scheduled banks.

In order to enlist the indigenous bankers as regular constituents of the modern money-market, steps should be taken to link them directly to the Reserve Bank of India. The Reserve Bank should prepare a list of such indigenous bankers as may have direct relations with it like scheduled banks in matters of loan advances and discount facilities, provided they register themselves under the Indian Companies Act prior to their transacting direct business with the Reserve Bank of India. A minimum aggregate amount of paid-up capital and reserve should be laid down as a condition for including them in the approved list, and to us it appears that a limit of rupees one lakh or over may be a useful guide, a paid-up capital and reserve

of rupees five lakhs or over being the criterion of including a commercial bank in the list of scheduled banks.

To obviate the difficulty of excluding the smaller indigenous bankers from the above privilege, it is suggested that local indigenous bankers should amalgamate themselves into units, which will conform to the test to be laid down by the Reserve Bank of India to be included in its list.

Every scheduled bank is obliged to maintain with the Reserve Bank of India a balance the amount of which shall not at the close of business on any day be less than five per cent of the demand liabilities and two per cent of the time liabilities of such bank in India, and is also obliged to furnish weekly, and in special cases monthly, returns to the Reserve Bank showing its financial position. These provisions should be dispensed with in the case of listed indigenous bankers, because maintaining any percentage of their assets as a balance with the Reserve Bank of India is likely to press hard upon their limited financial resources, nor are the indigenous bankers equipped with such an elaborate staff as may prepare regular weekly or monthly returns. In return of the privileges

which the listed indigenous banks will obtain as any other scheduled bank from the Reserve Bank, the latter should institute a regular system of audits over the indigenous bankers. The indigenous bankers should be made to keep their accounts and books in the manner prescribed by the Reserve Bank which must be permitted free access to such books and accounts whenever required. The Reserve Bank will do well to advise the indigenous bankers to reform their methods on modern lines. As a condition of their being included in the list, the Reserve Bank should insist upon the indigenous bankers to keep their short-term loan transactions entirely separate from those of long-term in separate sets of books and accounts, and they should also be persuaded to concentrate more upon short-term credit business, leaving the long-term one to the sphere of other more suitable long-term credit agencies as described in a subsequent chapter. The Reserve Bank will do well to insist that a portion of their assets bearing a fixed percentage to their total liabilities in short-term transactions should be kept in very liquid resources. The Reserve Bank should advise them as to the proper securities against which the indigenous banks may advance loans

consistent with safety and prudence, and in this connection definite encouragement should be given to the development of bills. The Reserve Bank may also insist upon the allocation of a fixed percentage of their net profits to the reserve fund. Various other lines of reform should be left to the Reserve Bank of India for working out in the course of actual working.

Thus reorganised the indigenous banks will inspire confidence and attract a bigger volume of deposits. It will be a good plan for the commercial banks to utilise such listed indigenous bankers in various local areas as their agents by entering with the latter into a partnership on what is known in Germany as the "Kommandit" principle, under which, instead of opening a branch in a place, a bank becomes the financing partner of a local private credit agency, whose advantages of local experience and knowledge are thus retained without involving the bank in the expense and heavy liabilities of a new branch.

CHAPTER II

SHORT TERM AND INTERMEDIATE CREDITS

In the previous chapter we have examined and suggested how the Reserve Bank of India can help in the provision of short-term agricultural credit for periods not exceeding nine months. But there are some short-term loans which we have termed as intermediate credit required by agriculturists for the purchase of expensive implements and cattle and for marketing. These short-term loans may be repayable either immediately after the harvest is over or over a period of years not exceeding three years. The Reserve Bank of India Act, 1934, has made no provision for the supply of intermediate credit for periods not less than nine months and not more than three years, and we shall now suggest how the Reserve Bank of India Act may be so amended as to cater for the intermediate credit needs of the agriculturists. The marketing credit needs of the Indian agriculturists are considered along with the inter-

mediate credit needs, because though marketing finance may be required for periods not exceeding nine months in which instance accommodation can already be obtained from the Reserve Bank of India, it will serve the marketing interests of the agriculturists in a more effective manner if the marketing credit can be available for a longer period, say, not exceeding three years.

The marketing conditions of the Indian agriculturist are far from satisfactory. He markets his produce under very disadvantageous circumstances. There is no orderly and regulated market for agricultural produce. Scales, weights and measures are manipulated against the agriculturist, who being single and poor has no remedy. The absence of standardized weights, measures, inspections and grading has rendered his position still worse. The lack of knowledge regarding supply and demand is a serious handicap for him. Difficulties of transport, high railway freights, etc., have further added to the problem. Last but not least in importance is the financial aspect of marketing, specially in India where the bulk of the agricultural produce finds its market internally within the country. In the majority of cases, the

agriculturist is forced to market his produce at an unfavourable price, because of his poverty, and his inability to hold on to his harvest for better prices. The farmers require finance to enable them not to unload their stuff all at the same time and thus depress prices. The wholesale and retail dealers all require finance to carry on their functions.

Agricultural marketing is financed in various ways in different provinces. The system of advances on crops, which is widely prevalent throughout India, has a very important bearing on marketing. Such advances carry high rates of interest and oblige the cultivator to sell his produce for less than the market price. Immediately the harvest is over, continual pressure is brought to bear upon the agriculturists to sell their produce all at the same time and thus depress prices in order to pay off their loans and debts.

Agricultural marketing finance also covers all the interest charges, which are paid by various middlemen for obtaining the necessary credit for moving the crops forward. The petty village dealers obtain their finance mostly from town merchants, shroffs and commission agents, who usually charge high rates of interest. The

small traders and village money-lenders, who buy agricultural produce directly from the cultivators, pay the latter on a cash basis. When these traders and money-lenders require more funds, they borrow in forms of actual cash from urban centres from larger traders or urban indigenous bankers or money-lenders. This arrangement has no direct contact with the money-market, and steps should be taken to link these financial transactions to the money-market by replacing cash transactions by means of hundis, which will be discounted in the money-market and rates of interest for such financial accommodation may thereby be reduced.

Darshani hundis are commonly drawn for obtaining funds in sending agricultural goods from one middleman to another. These hundis are either clean or backed by railway receipts, and funds are advanced by banks against these hundis. The banks generally prefer hundis supported by railway receipts. But some consignees insist on railway receipts being sent to them direct as a matter of prestige or to take an advance to pay the hundi or to save demmurrage. The traders also borrow funds from the money-lenders and indigenous banks on hundis,

which may in their turn be discounted by banks. The banks also make advances against the security of produce deposited in the godowns of the banks. The mercantile firms of Calcutta finance the movement of produce through their purchasing agencies or branch offices in the mofussil centres. The wholesale dealers of Calcutta obtain accommodation generally by borrowing from the banks on personal credit. Encouragement should be given to the drawing of funds more through hundis than in forms of cash. A large class of traders and merchants tend to remain outside the sphere of the banks, owing to their disinclination to pledge stocks with banks, and rigidity of the regulations governing advances by banks against the security of goods in the godown of the banks and the publicity given to such advances. With educative propaganda and persuasion and improvements effected in the godown conditions of the banks, the traders and merchants may be induced to take all steps to use the liquid goods in their possession for getting cheaper accommodation from banks. The joint-stock banks and the Imperial Bank of India should adopt a still more liberal policy in the matter of granting advances against agricultural produce in godowns.

In order to encourage the use of bills to secure financial accommodation from banks, and to encourage advances by the latter on the security of agricultural produce, it is necessary to provide for facilities for storage accommodation throughout the country by establishing suitable warehouses. Receipts issued by warehouses should serve as credit instruments on which accommodation may be obtained either from banks or other credit supplying agencies. The Reserve Bank of India should also make advances against warehouse receipts, and hence it is desirable that the Reserve Bank ought to possess some control over those warehouses, whose receipts will be considered good security for making advances.

The establishment of suitable warehouses is a fundamental requisite in marketing finance. They will also enable the cultivators to withhold their supply from the market if the price is unsatisfactory. The main difficulties in connection with storage and warehousing would be grading and mixing of stocks of different parties. But if the Indian cultivators can be made to realise the benefits of standardization, grading and pooling, and if they can obtain cheaper financial accommodation

through warehouse receipts they will before long respond to these improved practices. The establishment of warehouses should not be left to private individuals who may not find it profitable to build warehouses, involving as they would expenses and scientific treatment. In some provinces their respective governments are taking an active part in the building of warehouses by advancing part expenses. To us it appears that the task of establishing enough suitable warehouses should be undertaken by the Reserve Bank of India through its Agricultural Credit Department in collaboration with the Imperial Council of Agricultural Research which ought to place all its scientific resources at the disposal of the Reserve Bank for tackling the problems of grading, storing against damages, etc., involved in warehousing. Experiments may well be started in centres, where transport facilities are already available. The Reserve Bank should also control the management of these warehouses, whose receipts will thereby become first class credit instruments. The costs of such werehouses should be met out of the profits accruing to the Issue Department of the Reserve Bank of India. Profits

from note issue should rightly belong to the public, and their utilisation in some public service like the warehouses deserves to be considered. The initial costs of building the warehouses should be defrayed by the Reserve Bank of India from loans to be raised by its Agricultural Credit Department through some suitable methods. In the initial stages and even later if finances permit the cultivators should have free facilities for storage in warehouses. In no case should the warehouse cess, a charge for storage accommodation, be more than a nominal sum.

In addition to improving marketing finance simultaneous measures should also be taken to reform agricultural marketing in India on modern scientific lines. The extraordinary diversification and vagueness of marketing conditions throughout India and the ways in which produce contracts are drawn have rendered the financing of crops being left almost entirely either to the individual indigenous banker, or to importing and exporting houses with up-country agents. In order to overhaul the marketing conditions of agricultural products in India it is necessary to standardise the staples against which advances are made and similar standardisation

should be adopted regarding the contracts relating to them. Proper storing accommodation should be provided along with facilities for necessary insurance. The Agricultural Credit Department has also recommended that the possibility and desirability should be considered of creating throughout the country properly regulated forward markets run on orthodox lines in the interest of both sellers and buyers so that the value of produce may be hedged and the risk of violent fluctuations mitigated. Recently the Government of India has put on the legislative anvil a bill providing for experimenting with standardisation and storing, and these Governmental measures backed by the Imperial Council of Agricultural Research should have far-reaching effects. There must be provision for definite and easily realisable security for advances and this cannot be ensured unless there is grading or standardisation of staples so that goods can be described in brief and certain terms. The construction of licensed warehouses as previously discussed is also fundamental.

The Chief Marketing Expert with the Government of India working through the marketing officers in the various provinces should

go a long way towards improving the marketing technique of Indian agriculture in the form of marketing surveys, crop forecasts, specialisation, grading, etc.

The various measures suggested above will take time to materialise, and in the meantime the co-operative societies can play a very useful part. Co-operative godown societies and co-operative marketing have been tried with success in other countries, and they should be profitably introduced in India. Care should be taken to see that the co-operative godown and sale societies are prudently managed, and expert service should be utilised. Because storing and marketing involve not only costs, but also a great technical knowledge and skill, the management of these societies should be thoroughly acquanited with the conditions of supply and demand, especially of such commodities as wheat and cotton which command a world-wide market. Timely and accurate publication of crop forecasts by the Government should also greatly help agricultural marketing in India. The well-managed co-operative godown and sale societies could provide a very useful link between the individual agriculturist or the small dealers and the commercial banks.

Such societies, by providing a general collective guarantee over and above the top of the security actually offered by the commodity itself, would make it a commercial proposition for banks to make advances with narrower margins and in larger amounts.

The Reserve Bank of India Act, 1934, should be so ammended as to make provision for the supply of intermediate credit to agriculture through its Agricultural Credit Department for periods not less than nine months and not more than three years. The Federal Intermediate Credit System of the United States of America makes loans for periods not less than six months and not more than three years. The Intermediate Credit Banks are Government Institutions. Their establishment was made obligatory by an Act of the congress and the Secretary of the Treasury was directed to subscribe to their capital stock in such amounts as called for by the directors of the banks, not in excess of 5,000,000 dollars for each bank. To secure additional funds, these banks are empowered to issue and sell debentures secured by agricultural and live stock paper. In 1925 the Commonwealth Bank of Australia Act was so

amended as to create a Rural Credit Department, and to authorise the Bank to make advances through this Department to co-operative associations and other prescribed bodies upon the security of primary produce or land for periods not exceeding a year. The object was to introduce orderly marketing and to enable the cultivators to withhold their produce not for speculative purposes, but to improve and regulate the process of distribution throughout the year in the interests both of producers and consumers. Private individuals are not eligible for such advances, which are only made to associations of producers. No elaborate propaganda was needed to induce the producers to form associations, because pooling by private producers was already well developed, specially during and after the war. To provide funds for use by the Rural Credits Department the Act empowers the Federal Treasurer to lend to it up to £ 3 millions, and provision is also made for the issue of debentures by the Bank for funds. It has not been necessary to avail of these facilities. The Act also provided that 25 per cent of the net annual profits of the Note Issue Department of the Bank should be paid to the Rural Credits Department until

a total of £ 2,000,000 was reached. This amount was attained in September 1932, and represents the permanent capital of the Department. Any requirements above the Department's own resources are obtained from advances by the Bank. Profit making is not the aim of the Department, and hence out of the net profits accruing to the Department one-half is credited to the Rural Credits Department Reserve Fund and the other half to the Rural Credits Department Fund. The Act further provides that the latter Fund is to be used in such a manner as the Board directs, for the promotion of primary production. Similar provision should be made in the Reserve Bank of India Act.

The Reserve Bank of India Act, 1934, should be so amended as to authorise the Bank through its Agricultural Credit Department to make advances for periods not less than nine months and not more than three years. For this purpose the Agricultural Credit Department should be able to borrow from the Government of India a specified sum, and it should also be authorised to raise funds by floating debentures. It should be provided that 25 per cent of the net annual profits of the Note Issue Department of the Bank should be allocated to the Agricultural

Credit Department of the Reserve Bank of India till a certain amount of capital of the Department is built up. The Department should also have easy access to advances from the Bank. In addition to making advances to co-operative associations, banks and other prescribed bodies, the Agricultural Credit Department of the Reserve Bank of India should adopt the practice of making advances to private individuals at least until such time when individual producers have thoroughly organised themselves into associations, pools or the like. In the case of individuals, loans may be made further secure by providing that every loan application of a private individual should be accompanied with a suitable guarantor in the form of a primary credit society or a scheduled bank. Advances should be made upon the security of land or primary produce stored in the warehouses. In the absence of warehouse receipts, scheduled banks should be able to obtain such financial accommodation from the Agricultural Credit Department on the security of produce deposited in their own godowns, and then pass it on ultimately to the producers.

Like in the Commonwealth Bank of Australia Act, provision should be made to banish

profit-making from the Agricultural Credit Department of the Reserve Bank of India. The net annual profits of the Department when made should go to constitute a Rural Credit Reserve Fund as well as a Rural Credit Development Fund, the latter to be devoted to the promotion of Indian agriculture. In the beginning it will be desirable to allocate the entire profits of the Department to the Rural Credit Development Fund, which should be devoted for the first few years to the establishment of suitable warehouses in various parts of the country.

Chapter III

LONG TERM CREDIT

The Indian Agriculturists require long-term credits for substantial periods for various purposes, namely, the redemption of land, liquidation of old debts, improvement of land and cultivation, purchase of land, etc. The agriculturists' demands for long-term loans are almost continuous and unlimited. Owing to their heavy indebtedness the agriculturists are constantly pressed by their creditors to pay off old debts, which they not infrequently meet by raising a new loan. The absence of suitable long-term credit agencies have compelled the agriculturists to borrow from private sources at high rates of interest and under numerous disadvantageous conditions, which have in their turn imposed a chronic burden upon the agriculturists. The bulk of the incomes of the agricultural population go towards meeting their debt charges and obligations, and as a consequence they must incur fresh debts to carry on. The crushing burden of

agricultural indebtedness accounts for the chronic poverty of the rural population of India. Any measure calculated to improve the economic conditions of the Indian agriculturists must take cognisance of two factors, namely, the provision of suitable credit facilities as well as the application of additional remedies for eradicating the standing indebtedness of the cultivators. The problem of long-term credit in Indian agriculture involves concurrently the problem of wiping off the old debts, and we find in India that a step has been taken along right lines. The provision for facilities of long-term credit in Indian agriculture through the organisation of various land institutions like mortgage banks, loan offices, etc., has been harnessed to numerous measures of debt conciliation. The various provincial governments have lately been very active in enacting measures of debt conciliation and arbitration. In this chapter we shall confine our attention to an examination of the existing long-term credit agencies, and try to suggest how the latter may be further improved in co-ordination with the Reserve Bank of India.

As we have seen in a previous chapter, most of the agricultural credit agencies in India

finance both short-term and long-term loans, and this practice is unsound. Short-term and long-term credits involve problems different in nature and require separate treatment. Such is the practice in nearly all the progressive countries. In the provision of long-term credit facilities the State in various countries has taken an active part in providing its respective rural population with requisite land institutions. In Great Britain the Ministry of Agriculture and Fisheries with the sanction of the Treasury is authorised, under the Agricultural Credits Act of 1928, to contribute £ 10,000 towards the administrative costs of the newly established Mortgage Credit Corporation Ltd., and also to make advances not exceeding £ 750,000 free of interest for a period of sixty years for the formation of a Guarantee Fund. The Treasury is also empowered to subscribe to the debentures of the above Corporation to an amount not exceeding one-fourth of the net issue for £ 1,250,000 in all, and to procure the under-writing of the debentures up to a sum not exceeding five million pounds. The leading joint-stock banks in England, namely, the Bank of England, Barclays Bank Ltd., District Bank Ltd., Glyn Mills & Co., Lloyds Bank Ltd., Manchester and

Country Bank Ltd., Martins Bank Ltd., National Provincial Bank Ltd., Westminster Bank Ltd., and William Deacon's Bank Ltd., are the share-holding banks in this Land Mortgage Corporation. It should, however, be noted that the Commercial joint-stock banks of England could thus afford to lock up their resources in the shares of the Mortgage Corporation because of their unassailable position and huge reserve funds. It is laid down by the governing Act itself that the advances by the Corporation on agricultural mortgages must not exceed two-thirds of the estimated value of the property and must be repayabie by equal yearly or half-yearly instalments of principal and interest spread over a period not exceeding sixty years. The Corporation started work in January 1929, and has already a large volume of business to its credit. This Credit Mortgage Corporation of Great Britain is a limited liability concern on the joint-stock principle. The debenture stock of the Corporation is trustee security. The Federal Land Banks under the Federal Farm loan System of the United States of America give loans for periods ranging up to forty years. The funds of these land banks are raised by debentures. The Congress authorised the

Government of the United States: (a) to subscribe to the share capital of these banks and to take up their debentures to a specified amount; (b) to pay for organisation expenses up to 100,000 dollars; and (c) to make temporary deposits for the use of any such bank. The debentures of the Federal Land Banks are trustee securities, and the Federal Reserve System is authorised to buy and sell farm loan bonds. In addition, the Federal Land Banks are also recognised as depositories of public money. In New Zealand a "Long Term Mortgage Department was annexed to the New Zealand Bank by a special enactment in 1926. The Department has a special share and debenture capital. Debentures may be raised up to three times the amount of the special share capital, and are secured against long-term mortgage loans ranging up to 36½ years on an amortisation basis with interest at 6 per cent plus provision for sinking fund. The special share capital was raised by the issue of shares to the shareholders of the Bank of New Zealand. The Dominion Government derive a dividend of 6 per cent on their preferential shares while the other share-holders get 7½ per cent.

Experience records that for the purpose of long-term credit in agriculture land mortgage banks are the most suitable agencies. Different types of land mortgage banks with varying features are evolved in different countries in order to meet particular local needs rather than as a result of any definite economic theories. Land mortgage banks may be co-operative, non-co-operative or quasi-co-operative, the last lying in between the two former types. The Prussian Farm Mortgage Mutual Credit Associations represent co-operative types, being associations of borrowers. They have no capital. Their rates of interest are low, and profit-making is not their objective. Each member pays a small entrance fee to meet the necessary expenses, initial costs of land valuations and other incidental charges. They raise capital by issuing mortgage bonds bearing interest, and these bonds are regarded as perfect types of secure investment, they being quoted on the stock exchanges throughout Germany. These Landschaften are now unified into a "Central Landschaft" which performs the function of a central co-operative organisation. The Federal Farm Loan Banks of the United

States of America also belong to the co-operative type. The Credit Foncier de France represents the non-co-operative type of land mortgage banks. A large number of them have sprung up in several European countries on the French model. They are based on commercial and joint-stock principles. They work for profits and declare dividends. The State imposes certain restrictions on them in the interest of borrowers and debenture holders. The Agricultural Bank of Egypt also represnts the non-co-operative type. The quasi-co-operative type of land mortgage banks combine both commercial and co-operative principles in varying degrees. They are associations of borrowers and non-borrowers with share capital and on a limited liability basis though each member has only one vote irrespective of his share capital. They tend to keep dividends at a low figure. The Hungarian Land Mortgage Institutes consisting of large land owners, and the Hungarian National Small Holdings Land Moatgage Institutes comprising of small land owners represent the quasi-co-operative types.

During recent years land mortgage banks are being established in various provinces in

India. They are generally founded under the Co-operative Societies Act on co-operative principles, though in several cases the land mortgage banks based on the co-operative type have been found to contain an admixture of both co-operative and non-co-operative principles, by taking within themselves non-borrowers. The latter provide the land mortgage banks with capital, business ability and working experience. But the tendency is fast developing to eliminate them gradually in order to make these land mortgage banks full fledged co-operative institutions. Madras leads in co-operative land mortgage banks, where the movement has been daily gaining ground. About twelve years ago Madras started the experiment of land mortgage banks by establishing ten such banks, which were founded on a limited liability basis with a share capital, the borrowing power limited to a multiple of the paid-up capital, ordinarily 8 to 10 times. They were authorised to raise funds by issuing debentures against mortgages given them for obtaining loans. The Government of Madras agreed to purchase 6½ per cent debentures equal in value to those which the banks were able to sell in the market, subject to a limit of Rs. 50,000

for any one bank and Rs. $2\frac{1}{2}$ lakhs for the entire Presidency. Many of these banks failed to market their debentures, and it was found that the issuing of debentures by the several banks individually militated against the success of debenture issues. Hence, on the recommendation of the Townsend Committee on co-operation a Central Land Mortgage Bank was established, which became the financing and balancing centre for all the primary land mortgage banks. The Central Land Mortgage Bank was instituted with the specific object of financing the primary land mortgage banks by centralising the debenture issues. The Madras Gevernment lent to the Central Bank Rs. 15,000 free of interest for initial working capital to be repaid in the course of a few years. They have also guaranteed interest up to 6 per cent on all debentures floated by the Central Bank in the first five years up to the limit of Rs. 50 lakhs, but for the full term of the issues. The Government also extended to the Bank other facilities in administration by lending their expert staff to it. The primary mortgage banks are to transfer their mortgages to the Central Bank, which should issue debentures with a floating charge on all such

mortgages. In practice the working of the Central Land Mortgage Bank has been crowned with success. It has succeeded in financing the primary land mortage banks by raising its own funds through the issue of debentures, which are also trustee securities. Its debenture issues have met with a ready response from the investing public, and those debentures are considered as safe and secure investment, and they are in great demand from the Insurance Companies, Local Boards, individuals, co-operative banks, etc. The debenture issue limit of fifty lakhs of rupees, interest and capital of which are guaranteed by the Government has been reached, and the Central Land Mortgage Bank is seeking for a still larger amount. Five co-operative land mortgage banks have been recently established in Bengal under the Co-operative Societies Act. The capital has been sanctioned to be raised by issuing debentures by the Provincial Co-operative Bank, Bengal having no Central Land Mortgage Bank. The movement lies as yet in its experimental stage in Bengal. Similar co-operative land mortgage banks have been established in other provinces either with or without a central land mortgage bank as a

balancing and financing centre. The practices of these co-operative land mortgage banks vary widely in different parts of the country. Different provinces present varying methods of raising capital by debenture issues, repayment of loans, making loans for specified objects, management, etc. In general, it is found that in the majority of cases the Governments of respective provinces encourage actively in the growth of the land mortgage banks by guaranteeing the interest or capital or both of the debentures of land mortgage banks, and in some cases they even subscribe to such debentures and finance the land mortgage banks by loans. In addition to advancing part expenses of such banks in the initial stages of their working, the Governments provide them with proper staff, audit and control. The loans given by the land mortgage banks are usually devoted to the redemption of land and houses of the agriculturists, liquidation of old debts, improvements of methods of cultivation, etc.

In order to make the institution of land mortgage banks a more effective instrument of financing long-term agricultural loans, measures ought to be taken to unify the practices of the land mortgage banks throughout India in

the light of experiences already gained, providing at the same time for variations where local conditions so demand, and some link should be established between the land mortgage banks and the Reserve Bank of India.

For the provision of long-term credits to agriculturists the establishment of land mortgage banks is fundamental. The banks should be based on co-operative principles. Co-operation implying acting together in combination for mutual benefits is essential for the Indian cultivators with limited resources for obtaining requisite loans by offering joint securities. In every province there should be an apex Central Land Mortgage Corporation with as many primary co-operative land mortgage banks as required operating over fairly large areas for which purpose a district may be taken as a unit. Primary land mortgage may also have branches and agencies in remote rural areas. The chief function of the Central Corporation would be to finance the primary land mortgage banks, and it will raise its funds mainly by issuing debentures against mortgages transferred to it by the primary banks which have accepted them for giving loans. Centralisation and unification of debenture issues is the principal objective of

any Central Corporation. It will also have a share capital, which should be subscribed by its member primary land mortgage banks. In the absence of a central debenture issuing institution, the raising of funds by individual primary banks through debentures has not met with much success as in case of Madras prior to its having a Central Land Mortgage Bank, because such individual debenture issues overflood the market, and they do not carry the same degree of security as the debentures of a central issuing institution. The Central Mortgage Corporation should be restricted in its power of issuing debentures, which should bear a certain multiple of the value of the mortgages transferred to it by the primary mortgage banks. It should be an entirely distinct organisation from that of the apex provincial co-operative bank. The Provincial Co-operative Banks of Bengal, Bombay and the Punjab are now authorised to finance the primary land mortgage banks through the issue of debentures. Such practices should be abandoned as soon as possible, and a Central Land Mortgage Corporation ought to be established in each province to centralise the debenture issues and finance the primary land mortgage banks.

The co-operative land mortgage banks should possess a share capital, to be raised from the members, and this can be done in two ways. Any intending borrower may initially subscribe to the share capital before obtaining any loan or the share capital may be raised by deducting a certain percentage of the amount borrowed by a member at the time of the loan is advanced, five per cent being the practice in the United States of America. The latter system of raising the share capital is practised in the Madras Presidency, and should be followed in other parts of India.

In transacting business the primary land mortgage banks must be more business-like than the co-operative credit societies, because the methods of land mortgage banking are more difficult and technical. The maximum borrowing capacity of a primary land mortgage bank should be limited to a percentage of the value of the mortgage property which it can deposit with the Central Land Mortgage Bank. The primary land mortgage bank should advance to indivivual members an amount not exceeding half the value of the mortgaged property given as security, and no loan should be given which does not pay even its cost of administration.

The primary bank should carefully scrutinise the object of the loan which should not be for any unproductive purposes, examine the repaying capacity of the borrowers, and make a proper valuation of the mortgaged property with the help of an expert staff to be supplied by the Reserve Bank of India. Advances should usually be made for various periods not exceeding thirty years, which should gradually be extended to sixty years in the course of working. The repayment of loans should be made either by equal periodical instalments, generally annual, or by a gradual instalment system according to needs. The latter appeals more in areas where the cultivator must wait before a return can be obtained from the investment of the loans thus incurred.

In the initial stages the establishment of land mortgage banks needs particular encouragement and financial assistance. The respective provincial governments should defray part expenses of such banks including the central land mortgage banks in the beginning of their working. In this matter the Central Government should extend some financial aid to the provincial governments, and an allocation from the Rural Development Fund of the

Government of India may well be made for this purpose.

The respective provincial governments should guarantee both the interest and capital of the debentures of their land mortgage banks in order to inspire the confidence of the investing public. With a view to stamping such debentures with greater security and better marketability the land mortgage banks should be given powers of recovery by foreclosure and sale of the mortgaged property without the intervention of civil courts in cases of default of repayment by the mortgager. The interests of the aggrieved party ought to be simultaneously safeguarded by conferring on them the right to question in the civil courts the action of the banks and take any further steps in order fully to preserve their rights. Various provinces like the Punjab, the United Provinces, Central Provinces and the centrally administered areas have passed different Land Alienation Acts restricting the free transferability of agricultural lands. An alteration should be made in the Land Alienation Acts conferring free rights of transfer upon the land mortgage banks, which should be required to restrict the sales of land to agricultural classes. The debentures of land mortgage banks should

be made trustee securities. The various governments may be induced to purchase any unsubscribed portion of the debentures, but such a contingency is not likely to arise if the institution of the land mortgage banks is properly organised as in the case of Madras.

The procedure adopted by the existing Co-operative Land Mortgage Banks as regards the flotation of debentures appears to us unsatisfactory in two respects. These are generally issued in small lots at frequent intervals with varying dates of maturity to meet requirements. Second defect is the practice of making them redeemable at any time which tends to keep down their price at or below par, thereby discouraging investors who are deterred by the possibility of capital depreciation without a corresponding chance of appreciation. The popularity of these debentures would probably be increased if the Land Mortgage Banks were to utilise the funds which accrue to them by the repayment of the instalments on their loans to maintain the stability of the price of their debentures by open market operations. Mortgages issued by such institutions have generally to be repaid in equated instalments. On the other hand, debentures have to be issued with

a fairly long maturity before the first option to repay accrues. It is a common practice of mortgage companies in other countries to utilise the funds which thus come to their disposal to buy up their debentures in the open market, thus maintaining a steady price for them and increasing their popularity with the genuine investor, because he knows that he has a better chance of realising his holding without serious risk of loss when he so desires.

Some link should be established between the Reserve Bank of India and the land mortgage banks. It is sometimes suggested that the Reserve Bank of India should buy the debentures of land mortgage banks. We are definitely against any such proposal, because the assets of the Reserve Bank must always be kept very liquid and easily realisable, and hence it cannot afford to invest its funds in debentures, whose repayment must needs be spread over a considerable number of years. It is also unnecessary to load the Reserve Bank of India with a new Land Mortgage Department with separate share and debenture capital for financing the land mortgage banks when the existing land mortgage banking organisation may be utilised effectively to serve all useful purposes. To improve the

present situation we should suggest that the Reserve Bank of India may usefully undertake to float the debentures of the central land mortgage banks in their behalf. Being in close and constant touch with the money market, the Reserve Bank of India knows best which will be the most suitable time for floating the debentures at the lowest possible rates of interest. The Reserve Bank can also tap a wider source of finance than an ordinary central land mortgage bank. The association of the Reserve Bank of India with the flotation of such debentures will invariably impart to the latter a stamp of greater security. In so floating the debentures of the central land mortgage banks, the Reserve Bank of India must possess some control over their working. The books and accounts of the land mortgage banks should be open to inspection and audit by the Reserve Bank of India, which should also advise them as to how to improve their methods of business on safe and sound lines. The Reserve Bank of India will also do well to make periodical examination of the loans given by the land mortgage banks, and of the financial conditions of the parties to whom such loans have been advanced. The problem of valuation is of fundamental

importance in land mortgage banking, and a very useful service may be performed if the Reserve Bank of India in collaboration with the various Governments can supply the land mortgage banks with the requisite expert staff for valuation purposes.

The movement of land mortgage banking has hitherto received little attention in the majority of the provinces, and hence a more vigorous line of action should be pursued for the development of land mortgage banks throughout India. Given proper encouragement for their establishment, and provided improvements on the above lines are effected, the land mortgage banks will before long become the most effective instrument of supplying the rural areas with long-term credit. In the beginning the bulk of the advances made by these banks is likely to go towards paying off the old debts of the agricultural population, thus relieving the Indian cultivators of an old oppressive burden.

The co-operative land mortgage banks are likely to leave outside their scope a limited section of the agricultural interests, e. g., the zemindars, the land-holding classes and the like, who do not like to be included in any co-operative effort, which embraces mainly the small

agriculturists. The landlords also require credit, particularly in Bengal where the Permanent Settlement prevails. Hitherto, they have been financed by the various existing credit agencies at high rates of interest. Where the zemindars devote their loans to productive purpose of land improvement and the like, it is necessary to provide them with such productive credits at reasonable charges. Land Mortgage banks on the joint-stock principle have been evolved in several parts of the world for financing the land-owning classes. For example, the Credit Foncier de France is a joint-stock land mortgage bank, which advances sums up to 40,000 francs repayable in 25 years at low rates of interest. It acts as an apex bank for the regional mortgage banks throughout France. The Hypothee Bank of Japan advances long-term loans for periods not exceeding fifty years on the security of land. The Agricultural Land Mortgage Credit Corporation Ltd. of England is another instance of a joint-stock agricultural bank. The joint-stock Agricultural Bank of Egypt was founded in 1902. The Bank could advance to small farmers up to £ 20 each for not more than 15 months without any mortgage, and also not more than £ 300 each against a first mortgage for a period

not exceeding 5½ years. Interest was limited to 9 per cent. The bank issued £ 4½ million of bonds, on which an interest of 3½ per cent was guaranteed by the Egyptian Government, which also undertook to provide in any year such sum as might be necessary, after meeting all present claims and exhausting the reserve fund, to make up a profit of 3 per cent on the capital invested in loans. Within the first few years of its working the bank's policy of extending to cultivators cheap and facile credits failed. Loans were frequently taken for unproductive objects, and as a consequence the borrowers defaulted in repayments. The bank had to adopt a policy of foreclosure on the mortgage with the sale of the land. The maximum limits for the two classes of above loans were raised to £ 200 and £ 1,000 respectively, the period for the latter class of loans was raised from 5½ years to 20 years under the "five-feddan" law passed in 1912. Since then the bank had been pursuing a more stringent loan policy. Barring a few joint-stock banks transacting mainly agricultural loans in Northern India, the example of a purely agricultural joint-stock bank in India can be found in the Dawson's Bank, operating in the Irrawaddy Delta

of Burma. The bank is purely a private venture, and it advances loans on first mortgages, or against crops. The success of the bank has been due among other factors to its favourable localisation in an area, where harvests are secure, land valuable and easily marketable, and competition is limited.

For the purpose of financing the credit needs of that section of the agricultural population in India, which tends to remain outside the fold of a co-operative organisation, the institution of a joint-stock land mortgage bank on the above lines is recommended. In case the provincial governments decide to take an initiative to give a start to such banks they should be allowed to raise their working capital both by shares and debentures. The interest and capital of the debentures ought to carry the guarantee of the Government, which should possess a proper degree of control over such banks in matters of management, direction, audit, etc. The debentures should also be made trustee securities. In Bengal the need for such a new joint-stock land mortgage bank may be obviated by reforming the existing loan offices. The loan offices in Bengal are modelled on the land mortgage banks. There are 782 of

them working in Bengal in 1929, of which only 29 were in Calcutta. They had a total working capital of about Rs. 9 crores. The paid-up capital is usually small, only 13 having a paid-up capital of Rs. 1,00,000 or more. Their reserve funds bear generally a small percentage to their paid-up capital. The interest rates charged by them vary from 12 to 18 per cent. Their main function is to finance the Zemindars and other classes of the agricultural population against land, ornament or personal security. The methods employed by them, and the practices of the several loan offices differ widely. Owing to their small reserve funds and bad management, many loan-offices came to grief under the present conditions of economic depression. A very useful service may be done by reorganising and reforming the existing loan offices in Bengal either by a new "Loan Offices Act" or some such legislative enactment. The new legislation should provide for the following. A loan office should possess a subscribed share capital equal to at least one-half of its authorised capital. The Bengal Provincial Banking Enquiry Committee viewed with alarm the existence of numerous small loan offices, and they suggested amalgamation on the following

lines. A. minimum subscribed capital of Rs. 50,000 should be prescribed for small banks and loan offices. They also recommended that for the existing loan offices having a lower paid-up capital, legislation should be passed on the lines of the Indian Life Assurance Companies Act requiring a deposit of securities with Government of an amount by which their paid-up capital falls short of Rs. 25,000. Loan offices should not be allowed to advance money against their own shares as is the prevailing practice. They should be regarded as banks entitling them to all the privileges of banks, and they should be prevented from combining banking with other kinds of subsidiary business. They should draw up proper balance sheets and profits and loss accounts. Both the Bengal Provincial Banking Enquiry Committee and the Central Banking Enquiry Committee favoured some kind of control and regulation over the reserves of the loan offices. We should suggest that till a reserve equal to at least the paid-up capital of each loan office has been built up, the net annual profits of every loan office should be allocated to the reserve fund during the first five profit making years, and thereafter at least 25 per cent of such net

annual profits should go to the reserve fund. The provision of a permanent amount equal to 10 per cent of the net annual profits of any loan office for its reserve fund should be seriously considered in view of the fact that the paid-up capital of the loan offices is usually small. Regarding the investment of their reserve funds, the Bengal Banking Committee recommended that the loan offices in the mofussil should be allowed to open post office savings bank accounts and should have the same facilities regarding withdrawals as the co-operative societies. The maximum holding of postal cash certificates in the case of the mofussil loan offices should be raised to Rs. 20,000, but no charge should be made with regard to the accrual of interest on such certificates. Any surplus of reserves left after investing in post office savings banks and postal cash certificates should be invested in trustee securities.

It is necessary to emphasise here that before rehabilitating the credit of the agriculturist, it is imperative to devise suitable methods for removing or reducing his accumulated debt to an extent which will make it possible for him to liquidate it from his own resources.

The Agricultural Credit Department of the Reserve Bank of India has rightly suggested in its report that where indebtedness has grown beyond any reasonable capacity of the debtor to pay, the debt must be reduced either in respect of the capital amount or the rate of interest or both. Even if such reduction is voluntary, Government action will be required because the number of creditors who are likely to accept a voluntary reduction in their debts without some direct or indirect *quid pro quo* being offered by the Government would be inconsiderable. Reduction should be voluntary where possible, because compulsion may have far-reaching effects on credit generally, and on the morale of both debtors and creditors. Creditors are expected to accept considerable reductions if the Government is prepared to compensate them in the form of simplifying the legal procedure for recovering the reduced debt, when it has been assessed by an independent conciliation authority as within the debtor's capacity to repay, or if the capital and the interest so assessed are supplemented by some form of direct or indirect Government assistance regarding repayment. The experiment of tackling the problem of rural

indebtedness through the mechanism of conciliation boards has succeeded in the Central Provinces, and similar conciliation boards should be tried in other provinces as well. The Agricultural Credit Department further suggests that Provincial Governments might consider the possibility of providing some regular machinery whereby the long-term debts settled by the conciliation boards could be recovered in small instalments with provision for the levy of additional collections in good seasons. In the case of those whose debts cannot be reduced by voluntary agreement within their capacity to repay and whose assets are inadequate to cover the debt, the various provinces should consider the desirability of enacting simple Rural Insolvency Acts, and in this connexion attention may be drawn to the provisions of the Bengal Agricultural Debtors Act, 1936. The Agricultural Credit Department also suggests the enactment of emergency legislation for preferential treatment to hereditary liabilities, say, of over 30 years' standing. Such hereditary liabities as are handed down from generations under social traditions and customs present one of the greatest obstacles to the economic regeneration of the rural areas.

Once the credit of the agriculturist has been improved by reduction or removal of his debt, suitable measures and checks must be devised to safeguard him against falling heavily into debt again. Though education appears to be the only real and lasting corrective, under existing conditions it must be a slow process. It will require continuous efforts for years to educate the peasant out of his ingrained habit of improvidence. The peasant should be prevented from utilising his restored credit for unnecessary borrowing. The Agricultural Credit Department rightly considers that legislation backed by educative propaganda should prove reasonably effective in curbing the tendency among the agriculturists to incur debts for purposes other than *bona fide* agricultural requirements. The same Department would like to see the credit of the agriculturist so restricted as to make it difficult for him to incur debt except for *bona fide* agricultural requirements and beyond his capicity to repay from his own resources, but that, subject to those limitations, he should be able to borrow at rates more in consonance with those prevailing in the money market. It is suggested that total future liability (after the liquidation of previous

debts) of agriculturists might be limited either by fixing it in terms of a suitable multiple of land revenue or on the basis of the average value of land held in proprietary or occupancy right so as to enable the debt to be liquidated, after providing for the bare necessities of life of the owner (tenant) and his family, within a period of, say, 30 years. In order to obviate any evasion the agriculturist money-lender should also be brought within the purview of enactments prohibiting or restricting the transfer of agricultural land. A further safeguard against excessive credit and evasion of restrictive measures would be to prohibit borrowing from more than one source.

CHAPTER IV

AGRICULTURAL CREDIT DEPARTMENT OF THE RESERVE BANK OF INDIA

In accordance with the provisions of the Reserve Bank of India Act, 1934, the Bank has created a special Agricultural Credit Department, but the Department is as yet in the preliminary stage and has hardly started working. The Reserve Bank Act provides that the Department shall maintain an expert staff to study all questions of agricultural credit and be available for consultation by the Governor General in Council, Local Governments, provincial co-operative banks, and other banking organisations. The Department is also empowered by the said Act to co-ordinate the operations of the Bank in connection with agricultural credit and its relations with provincial co-operative banks and any other banks or organisations engaged in the business of agricultural credit. In addition to its consultative and advisory duties the Agricultural Credit Department should possess

some active functions in the financing of Indian agriculture. The Reserve Bank of India Act has also imposed upon the Bank the duty of submitting a report with proposals for legislation, if necessary, within three years of its working upon (a) the extension of the provisions of the Reserve Bank of India Act relating to scheduled banks to persons and firms, not being scheduled banks, engaged in British India in banking business, and (b) the improvement of the machinery for dealing with agricultural finance and methods for effecting a closer connection between agricultural enterprise and the operations of the Bank. In this matter the Reserve Bank may be substantially assisted by its Agricultural Credit Department.

In the preceding pages we have suggested how the Reserve Bank of India can help in the supply of agricultural credit through the reorganisation of exiting credit agencies as well as by supplying directly intermediate credits through its Agricultural Credit Department. Be it remembered here that wherever we have suggested any measure to be adopted by the Reserve Bank of India for the better provision of agricutural credit, the Bank in almost all such cases will have to work through its Agricultural

Credit Department. The Department will have to pay particular attention to the development and expansion of the existing credit agencies, and attempt their consolidation, co-operation and co-ordination. They must be made to work in close harmony.

The Agricultural Credit Department should evolve a suitable audit staff, which will be entrusted with the task of imposing the necessary checks upon the co-operative, indigenous and land mortgage banks in the manner discussed in the previous chapters. The audit staff should consist of trained and experienced people. The Department should also try to provide for the training of the co-operative auditors, before they are appointed by the respective provincial governments in their own co-operative departments, and thus the present practice of the several provinces of getting the auditing and inspection work done by amateurs may be reformed with benefits to the co-operative movement. The Agricultural Credit Department should also provide the land mortgage banks with a valuation staff, because valuation work being fundamental for the successful working of land mortgage banks must be undertaken by experienced and competent people. The

Department should be entrusted with the task of establishing suitable warehouses in various centres throughout India.

The Agricultural Credit Department should make serious endeavours to develop a bill habit among the rural areas. The system of drawing hundis varies in different places. There is no legal definition of a hundi. It is governed by the custom and usages of various localities, and only where no specific custom exists does it come under the term "bill of exchange" within the meaning of the Negotiable Instruments Act. Hundis are of two kinds, *darshani* or demand bills, and *muddati* or usance bills. The Department should recommend the standardisation of the custom governing the hundis with a view to promoting their circulation, at least for particular regions if not possible for an entire province. The language of the hundis should be as simple as possible. The Agricultural Credit Department should seriously consider if the Reserve Bank of India should not discriminate between cash credits and discounts. We think it will help the bill habit among the Indian population if the Reserve Bank of India charges a slightly higher rate for its cash credits than its discount rate. The Agricultural Credit Department

should try to encourage the shroffs and other urban credit agencies to finance the village bankers by means of usance bills. In case of financing the cultivators the village bankers should adopt the system of drawing usance bills with dates of maturity approximately fixed, providing margin with reference to the probable date on which the crops would be brought to the market for sale, because the cultivators can only meet their bills with the proceeds of their sales.

Pressure should be brought to bear upon the Government to encourage the financing of agriculture through bills. The high rate of stamp duty is one of the main obstacles to the growth of bills. The Central Banking Enquiry Committee, 1931, recommended the abolition of the stamp duty. The same Committee also recommended that as an initial step the stamp duty on all bills of less than one year's usance should be reduced to a uniform rate of two annas per one thousand rupees. The large fall in the rate of interest since then has rendered the incidence of this taxation much heavier. The recent report of the Agricultural Credit Department of the Reserve Bank of India also recommends a reduction in the duty, and it points out that

the loss of revenues to the provinces should be small in view of the fact that the number of bills drawn at present is not great and should be, to a considerable extent, made up by the increase in the number of bills. The same report, therefore, confirms the findings of the Central Banking Enquiry Committee that the duty on bills of less than one year's usance should be reduced to two annas per thousand rupees. In America the stamp duty on bills of exchange was abolished on the inauguration of the Federal Reserve Bank System.

The Agricultural Credit Department should seriously consider the possibility of bringing the co-operative banks of the Native States of India within the scope of the Reserve Bank of India because they remain outside its scope under the existing Act.

The Agricultural Credit Department should study the problems of Nidhis and Chit Funds of Madras. There were 228 Nidhis in the Madras Presidency in 1929. Nidhis are founded with the object of relieving their members from old debts and giving loans at reasonable charges against good security. Non-members are not allowed to secure any loans as a general rule. The funds of the Nidhis are mainly obtained by

subscriptions of members to share capital. The characteristics of a large number of Nidhis are those of a terminating society of members who contribute monthly an amount which is available for loans to members. But this characteristic has largely disappeared. Some Nidhis have adopted the practice of a recurring deposit and a fixed small share capital which may or may not be withdrawn in place of the monthly subscription to share capital. The total money handled by the Nidhis comes to about Rs. 4 crores. The Nidhis are all registered under the Indian Companies Act, and some of them are carrying on regular banking business. They vary widely in their working and constitution, from joint-stock banks to mutual benefit societies and Chit Funds which are merely loose associations of a small number of people. The Chit Funds were developed for the purpose of providing their members with a lump sum to meet an unusual expenditure and also for facilitating savings. In spite of the successful working of the Chit Funds, some of them are full of abuses which ought to be removed. The Central Banking Enquiry Committee suggested a few lines of improvement on the model of the English Building Societies after which the

Nidhis are generally built. The Nidhis and Chit Funds in Madras should be controlled by a special act of the Madras Legislature called the "Nidhis and Chit Funds Act." The Nidhis which have developed into full fledged banks should be recognised as such for all purposes, entitling them to all the privileges of a bank as well as imposing upon them all the obligations of the latter. The Nidhis should all be registered. The Madras Government should make it obligatory for the promoters of Chit Funds to be licensed, and the Chit Funds should also be registered.

Being a bankers' bank, a central bank is not allowed to compete with other banks by having any open market operations. But in certain countries, especially where central banking institutions are of recent growth, the central banks have been invested with powers of doing open market operations, that is to say, they are allowed to deal directly with private parties in matters of loans and advances, and purchase, sale and discount of bills. Such powers of direct discount are expected to be utilised by the central banks only in cases of special emergencies, which necessitate the exercise of those powers in the financial interests of the

countries concerned. The Reserve Bank of India has also been invested with similar powers of direct discounts. The Reserve Bank of India Act provides in section 18 that when in the opinion of the Central Boards or, where the powers and functions of the Central Board under section 18 of the above Act have been delegated to a committee of the Central Board or to the Governor, in the opinion of such committee or of the Governor as the case may be, a special occasion has arisen making it necessary or expedient that action should be taken under section 18 for the purpose of regulating credit in the interests of Indian trade, commerce, industry and agriculture, the Bank may, notwithstanding any limitation contained in sub-clauses (a) and (b) of clause (2) or sub-clause (a) or (b) of clause (3) or clause (4) of section 17,—

(1) purchase, sell or discount any of the bills of exchange or promissory notes specified in sub-clause (a) or (b) of clause (2) or sub-clause (b) of clause (3) of that section though such bill or promissory note does not bear the signature of a scheduled bank or a provincial co-operative bank ; or

(2) make loans or advances repayable on demand or on the expiry of fixed periods not

exceeding ninety days against the various forms of security specified in clause (4) of that section. It is, however, mentioned in the same Act that a committee of the Board or the Governor shall not, save in cases of special urgency, authorise action under this section without prior consultation with the Central Board and that in all cases action so authorised shall be reported to the members of the Central Board forthwith.

Unlike other central banks the Reserve Bank of India will have to exercise its power of open market operations through direct purchase, sale and discount of bills, at least during the first few years of its working, more freely and more as its normal powers than emergency ones, owing to the peculiarly unique conditions of India. In India the bill habit is as yet undeveloped, and the Reserve Bank of India should take an active initiative in fostering the bill habit among the Indian population. In order to do so the Reserve Bank of India should have direct relations with the rural credit agencies. After careful scrutiny and selection the Reserve Bank of India should deal directly with indigenous banks, money-lenders, co-operative credit societies and co-operative central

banks, private individuals, etc., who are concerned mainly with agricultural finance, and thus the Reserve Bank will be able to popularise the bill habit among the rural areas. Under existing conditions the bulk of the rural credit agencies lies outside the scope of the Reserve Bank, and hence if some direct link could be established between the Reserve Bank and the rural credit agencies in matters of loans and advances, and purchase, sale and discount of bills, a great fillip would be imparted to the growth of bills in the rural areas. In this matter the Agricultural Credit Department of the Bank may substantially assist the latter as to the selection of those with whom the Reserve Bank may deal directly with safety as well as to the extent of such dealings. The Agricultural Credit Department should be fully posted with all requisite information.

The Agricultural Credit Department should recruit a suitable expert staff, which will be entrusted with great responsibilities. In addition to suggesting reforms and legislation on the lines of the preceding pages the Agricultural Credit Department should make a thorough study of the uninvestigated credit problems of Indian agriculture. One of the foremost duties of the

Department will be to give the right lead to the co-operative movement in India, co-operation being fundamental for the agricultural population. The co-operative movement in India has been vitiated by numerous defects. Hasty organisation, expansion without consolidation, inadequate supervision, defective audit, lack of care in lending, inattention to repaying capacity, tenderness in collection, excessive reliance on honorary work, utilisation of short-term deposits for long-term loans making thereby assets frozen, are some of the glaring drawbacks from which the Indian co-operative movement has been suffering. Immediate action ought to be taken on the recommendations of Mr. M. L. Darling, I.C.S., who recently made a thorough investigation of the whole subject. Some suitable schemes ought to be devised by which real principles of co-operation may be inculcated among the people. They should understand and feel that co-operation means membership in a living society. It further means common enjoyment. The democratic element of co-operation should be stressed, making everybody realise that all benefit in proportion to the use of which they make of their society. Along with other measures of reform, the Agricultural

Credit Department should insist upon an active agrarian policy to be pursued by the Government.

It is fundamental to remember that the provision of credit facilities will only solve a part of the major problem of agricultural India. In order to make the agriculturist creditworthy in the real sense of the term steps ought to be taken not only in the lines as previously suggested, but a dash should also be given towards what is popularly known as rural betterment. The General economic condition of the Indian farmer must be improved so that his earning power and purchasing capacity may be considerably enhanced. Economic rehabilitation of rural India must be accompanied by improvements in village sanitation and hygiene, the provision of ample medical facilities, the construction of roads, wells and irrigation works, the spread of education especially on vocational lines, and kindred other reforms. Co-operative action towards consolidation of holdings should be encouraged and further splitting up of holdings into uneconomic units should be prevented. Real and lasting improvement in the economic condition of the Indian farmer can be made and maintained provided steps are

taken to see that once the previous debt of the cultivator has been scaled down to his capacity to liquidate, his future borrowings are strictly confined and restricted to what is required for *bona fide* agricultural purposes.

APPENDIX I.

Business which the Reserve Bank of India may transact under the Reserve Bank of India Act, 1934.

Sec. 17. The Bank shall be authorized to carry on and transact the several kinds of business hereinafter specified, namely :—

1. the accepting of money on deposit without interest from, and the collection of money for, the Secretary of State in Council, the Governor General in Council, Local Governments, State in India, local authorities, banks and other persons ;

2. (a) the purchase, sale and rediscount of bills of exchange and promissory notes, drawn on and payable in India and arising out of *bona fide* commercial or trade transactions bearing two or more good signatures, one of which shall be that of a scheduled bank, and maturing within ninety days from the date of such purchase or rediscount, exclusive of days of grace ;

(b) the purchase, sale and rediscount of bills of exchange and promissory notes, drawn and payable in India and bearing two or more goods signatures, one of which shall be that or a scheduled bank, or a provincial co-operative bank, and drawn or issued for the purpose of financing seasonal agricultural operations or the marketing of crops, and maturing within nine

months from the date of such purchase or rediscount, exclusive of days of grace ;

(c) the purchase, sale and rediscount of bills of exchange and promissory notes drawn and payable in India and bearing the signature of a scheduled bank, and issued or drawn for the purpose of holding or trading in securities of the Government of India or a Local Government, or such securities of States in India as may be specified in this behalf by the Governor General in Council on the recommendation of the Central Board, and maturing within ninety days from the date of such purchase or rediscount, exclusive of days of grace ;

3. (a) the purchase from and sale to scheduled banks of sterling in amounts of not less than the equivalent of one lakh of rupees ;

(b) the purchase, sale and rediscount of bills of exchange (including treasury bills) drawn in or on any place in the United Kingdom and maturing within ninety days from the date of purchase, provided that no such purchase, sale or rediscount shall be made in India except with a scheduled bank ; and

(c) the keeping of balances with banks in the United Kingdom.

4. the making to States in India, local authorities, scheduled banks and provincial co-operative banks of loans and advances, repayable on demand or on the expiry of fixed periods not exceeding ninety days, against the security of—

(a) stock, funds and securities (other than immovable property) in which a trustee is authorized to invest trust money by any Act of Parliament or by any law for the time being in force in British India ;

(b) gold or silver or documents of title to the same ;

(c) such bills of exchange and promissory notes as are eligible for purchase or rediscount by the Bank ;

(d) promissory notes of any scheduled bank or a provincial co-operative bank, supported by documents of title to goods which have been transferred, assigned, or pledged to any such bank as security for a cash credit or trade transactions, or for the purpose of financing seasonal agricultural operations or the marketing of crops ;

5. the making to the Governor General in Council and to such Local Governments as may have the custody and management of their own provincial revenues of advances repayable in each case not later than three months from the date of the making of the advance ;

6. the issue of demand drafts made payable at its own office or agencies and the making, issue and circulation of bank post bills ;

7. the purchase and sale of Government securities of the United Kingdom maturing within ten years from the date of such purchase ;

8. the purchase and sale of securities of the Government of India or of a Local Government of any

maturity or of such securities of a local authority in British India or of such States in India as may be specified in this behalf by the Governor General in Council on the recommendation of the Central Board ;

9. Provided that securities fully guarantee as to principal and interest by the Government of India, a Local Government, a local authority, or a State in India shall be deemed for the purposes of this clause to be securities of such Government, authority or State ;

Provided further that the amount of such securities held at any time in the Banking Department shall be so regulated that—

(a) the total value of such securities shall not exceed the aggregate amount of the share capital of the Bank, the Reserve Funds and three-fifths of the liabilities of the Banking Department in respect of deposits ;

(b) the value of such securities maturing after one year shall not exceed the aggregate amount of the share capital of the Bank, the Reserve Fund and two-fifths of the liabilities of the Banking Department in respect of deposits ; and

(c) the value of such securities maturing after ten years shall not exceed the aggregate amount of the share capital of the Bank and Reserve Fund and one-fifth of the liabilities of the Banking Department in respect of deposits ;

9. the custody of monies ; securities and other articles of value, and the collection of the proceeds,

whether principal, interest or dividend, of any such securities ;

10. the sale and realisation of all properties, whether movable or immovable, which may in any way come into the possession of the Bank in satisfaction, or part satisfaction, of any of its claims ;

11. the acting as agent for the Secretary of State in Council, the Governor General in Council or any Local Government or local authority or State in India in the transaction of any of the following kinds of business, namely :—

(a) the purchase and sale of gold and silver ;

(b) the purchase, sale, transfer and custody of bills of exchange, securities or shares in any company ;

(c) the collection of the proceeds, whether principal, interest or dividends, of any securities or shares ;

(d) the remittance of such proceeds, at the risk of the principal, by bills of exchange payable either in India or elsewhere ;

(e) the management of public debt ;

12. the purchase and sale of gold coin and bullion ;

13. the opening of an account with or the making of an agency agreement with, and the acting as agent or correspondent of a bank which is the principal currency authority of any country under the law for the time being in force in that country or any international bank formed by such banks, and the investing of the funds of the bank in the shares of any such international bank ;

14. the borrowing of money for a period not exceeding one month for the purposes of the business of the bank, and the giving of security for money so borrowed ;

Provided that no money shall be borrowed under this clause from any person in India other than a scheduled bank which is the principal currency authority of any country under the law for the time being in force in that country ;

Provided further that the total amount of such borrowings from persons in India shall not at any time exceed the amount of the share capital of the Bank ;

15. the making and issue of bank notes subject to the provision in this Act ; and

16. generally, the doing of all such matters and things as may be incidental to or consequential upon the exercise of its powers or the discharge of its duties under this Act.

Sec. 18. When, in the opinion of the Central Board or, when the powers and functions of the Central Board under this sections have been delegated to a committee or of the Central Board or to the Governor, in the opinion of such committee or of the Governor as the case may be, a special occasion has arisen making it necessary or expedient that action should be taken under this section for the purpose of regulating credit in the interests of Indian trade, commerce, industry and agriculture, the Bank may, notwithstanding any limitation contained in sub-clauses (a) and (b) of clause (2) or

sub-clause (a) or (b) of clause (3) or clause (4) of section 17,—

1. purchase, sell or discount any of the bills of exchange or promissory notes specified in sub-clause (a) or (b) of clause (2) or sub-clause (b) of clause (3) of that section though such bills or promissory notes do not bear the signature of a scheduled bank or a provincial co-operative bank or

2. purchase or sell sterling in amounts of not less than the equivalent of one lakh of rupees ; or

3. make loans or advances repayable on demand or on the expiry of fixed periods not exceeding ninety days against the various forms of security specified in clause (4) of that section :

Provided that a committee of the Board or the Governor shall not, save in cases of special urgency, authorise action under this section without prior consultation with the Central Board and that in all cases actions so authorised shall be reported to the members of the Central Board forthwith.

Sec. 19. Save as otherwise provided in Sections 17, 18 and 45, the Bank may not :—

1. engage in trade or otherwise have a direct interest in any commercial, industrial, or other undertaking except such interest as it may in any way acquire in the course of the satisfaction of any of its claims : provided that all such interests shall be disposed of at the earliest possible moment ;

2. purchase its own shares or the shares of any other bank or of any company, or grant loans upon the security of any such shares ;

3. advance money on mortgage of, or otherwise on the security of, immovable property or documents of title relating thereto, or become the owner of immovable property, except so far as is necessary for its own business premises and residences for its officers and servants ;

4. make loans or advances ;

5. draw or accept bills payable otherwise than on demand ;

6. allow interest on deposits or current accounts.

APPENDIX II

Banks Scheduled to the Reserve Bank of India.

Ajodhia Bank, Fyzabad.
Allahabad Bank.
American Express Company, Incorporated.
Balthazar and Son, Rangoon.
Banco Nacional Ultamarino.
Bank of Baroda.
Bank of Behar.
Bank of Hindusthan, Madras.
Bank of India, Bombay.
Bank of Taiwan.
Bank of Upper Burma.
Benares Bank.
Bengal Central Bank.
Bhagwan Das & Co., Dehra Dun.
Canara Bank.
Central Bank of India.
Chartered Bank of India, Australia and China.
Comptoir National d'Escompte De Paris.
Comilla Union Bank, Calcutta.
Eastern Bank.
Grindlay and Company.
Hongkong and Shanghai Banking Corporation.
Imperial Bank of India.
Indian Bank, Madras.
Industrial Bank of Western India, Ahmedabad.

Jalpaiguri Banking and Trading Corporation.
Karnani Industrial Bank.
Llyods Bank.
Mercantile Bank of India.
Mitsui Bank, Bombay.
Nadar Bank, Tuticorin.
National Bank of India.
National City Bank of New York
Nederlandsche Indische Handels-bank.
Nederlandsche Handel-Maatschappij.
Nedungadi Bank, Calicut.
Oudh Commercial Bank.
Overseas Chinese Banking Corporation, Rangoon.
P. and O. Banking Corporation.
Punjab and Sind Bank, Amritsar.
Punjab National Bank, Lahore.
Quilon Bank, Quilon.
Simla Banking and Industrial Company.
Thomas Cook and Son (Bankers) Ltd.
Travancore National Bank, Tiruvalla.
Union Bank of India, Bombay.
U. Rai Gyaw Thoo and Co.. Akyab.
Yokohama Specie Bank.
Comilla Banking Corporation Ltd.
Punjab Co-operative Bank, Amritsar.

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